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LOCAL GOVERNANCE IN RURAL CHINA: AN ANALYSIS OF FISCAL, POLITICAL AND SOCIAL INSTITUTIONS

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Thesis submitted for the degree of PhD

2015

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Abstract

China is moving from a decentralized to a centralized system of government. Nowhere is this change in central-local relations more evident than in the rural areas. The analysis of the political, fiscal, and administrative dimensions of (de-)centralization at the village level reveals a paradox: the apparent empowerment of villagers to hold village officials accountable for service provision through elections and other democratic institutions contrasts with the parallel disempowerment of popularly elected village committees.

Using cross-sectional survey data from more than 100 villages in six provinces, this study investigates how the distribution of *power* (i.e., control over fiscal resources) between levels of the Party-state, and between Party and non-Party institutions at the village level, affects patterns of *accountability* and *participation* in service delivery across rural communities. The empirical analysis shows that in villages governed by democratically elected village committees, officials tend to be more accountable to villagers and to allocate more resources to the provision of infrastructure. However, village committees are powerless in most villages, even when – and especially when – they are democratically elected.

The findings suggest that, by undermining the power of village committees and ultimately the effectiveness of village elections, the centralization of the fiscal and administrative systems has contributed to a reversal of political decentralization and to a widening of the “accountability gap” between villagers and officials – a gap that cannot be filled by the Party’s control mechanisms alone, whether fiscal (e.g., earmarked transfers), administrative (e.g., performance contracts) or political (e.g., intra-Party elections). In parts of rural China, this has led to a decline in the legitimacy of the (local) state and to the growth of clan and religious organizations that substitute for the state in the provision of basic infrastructure services. Participation in these organizations is a symptom of, not a solution to, problems of local governance.

Table of Contents

1. Introduction.....	11
1.1. Research Objectives.....	12
1.2. Research Questions.....	14
1.2.1. Political Decentralization, Government Accountability, and Public Goods Provision.....	14
1.2.2. The Use of Transfers, Performance Contracts and Intra-Party Elections: Implications for Political Decentralization and Public Goods Provision	19
1.2.3. “Substitutive” Public Goods Provision by Self-Governing Organizations	23
1.3. Background.....	29
1.3.1. (De-)centralization in Rural China: Power, Accountability and Participation.....	29
1.3.2. Village Elections.....	30
1.3.3. Fiscal Centralization	33
1.3.4. Administrative Centralization.....	35
1.3.5. Intra-Party Elections	37
1.3.6. Participation in Local Governance	37
1.4. Methodology and Structure of the Thesis.....	38
1.5. The Data Set	42
1.6. Key Findings and Implications of the Study	43

2. China's Intergovernmental Fiscal Reforms and Rural Public Finance.....	47
2.1. Introduction.....	48
2.2. The Re-centralization of Intergovernmental Fiscal Relations	54
2.2.1. The Fiscal Contracting System	56
2.2.2. The Tax-Sharing System Reform	60
2.3. Interjurisdictional Competition.....	70
2.4. Rural Fiscal Reforms	77
2.5. Making Decentralization Partial?.....	81
2.6. Summary.....	89
3. Political Institutions and the Provision of Local Public Goods.....	92
3.1. Introduction.....	93
3.2. Power, Accountability and State Provision of Infrastructure	99
3.3. Hypotheses Development	105
3.3.1. Village Democracy	105
3.3.2. Intra-Party Democracy.....	113
3.3.3. Bureaucratic Control.....	116
3.4. Variables, Econometric Model and Estimation Method.....	123
3.4.1. Village Democracy and Village Public Goods Provision.....	125
3.4.2. The Cadre Responsibility System.....	132
3.4.3. Intra-Party Elections	134
3.4.4. Control Variables.....	135
3.4.5. Econometric Model and Estimation Method	137
3.5. Results and Findings	139
3.6. Summary.....	148

4. Social Institutions and Local Public Goods Provision.....	150
4.1. Introduction.....	151
4.2. Rural Social Organizations and Non-State Provision of Basic Services	156
4.3. Hypotheses Development	170
4.3.1. Political Trust.....	170
4.3.2. Local Government Performance	174
4.3.3. Lineage Ties.....	177
4.3.4. Labour Migration.....	179
4.4. Variables, Econometric Model and Estimation Method.....	182
4.4.1. Political Trust and Participation in Self-Governing Organizations	183
4.4.2. Local Government Performance	185
4.4.3. Lineage Ties and Migration	186
4.4.4. Control Variables.....	187
4.4.5. Econometric Model and Estimation Method	187
4.5. Results and Findings	191
4.6. Summary.....	196
5. Conclusion	201
5.1. Introduction.....	202
5.2. Main Findings	204
5.2.1. The “Accountability-Power Paradox” in Village Governance	204
5.2.2. Non-State Provision by Self-Governing Organizations: “Decentralization by Default”?.....	210
5.3. Contributions to the “Varieties of Governance” Literature	216
References.....	222

List of Tables, Boxes and Figures

List of Tables

Table 2.1: China's intergovernmental fiscal system	54
Table 2.2: Revenue assignments: central, local and shared taxes	61
Table 2.3: Expenditure responsibilities of central and local governments	62
Table 2.4: Classification of intergovernmental transfers	64
Table 2.5: Central-provincial transfers: vertical and horizontal shares	65
Table 2.6: China's central-provincial transfer system	67
Table 2.7: Types of central-provincial transfers (1995-2009)	68
Table 2.8: "Building a new socialist countryside": major programs	80
Table 2.9: Local share of revenues and expenditures (1980-2010)	82
Table 2.10: Vertical imbalance of rural governments	83
Table 2.11: Local share of revenues and expenditures in various countries	83
Table 2.12: Central transfers to local governments (2012)	83
Table 2.13: Forms of Decentralization and Public Service Delivery	85
Table 3.1: Proportion of investment in village public projects financed by higher-level governments before and after the tax-for-fee reform	101
Table 3.2: Variation in sources of funding for village public projects	102
Table 3.3: Distribution of power over the allocation of village funds	103
Table 3.4: Cadre-evaluation criteria in three townships	118
Table 3.5: Variation in village government expenditures on infrastructure	125
Table 3.6: Distribution of villages by level of election quality	128
Table 3.7: Distribution of villages by type of power structure	130
Table 3.8: Quality of elections and power of (elected) village committees	131
Table 3.9: Village democracy index scores, by province	132
Table 3.10: Policy mandates index scores, by province	133

Table 3.11: Township interference in the (s)election of Party secretaries	135
Table 3.12: Village democracy and village public goods provision: main model specification and hypotheses	138
Table 3.13: Results of the first-stage regression (main model)	145
Table 3.14: 3SLS estimates of the relationship between village democracy and village-financed investment (main model)	146
Table 3.15: 3SLS estimates of the relationship between village democracy and government-financed investment (additional model)	147
Table 4.1: Classification of village organizations by type of activity	158
Table 4.2: Classification of village organizations by degree of autonomy	161
Table 4.3: The role of village organizations in public goods provision	164
Table 4.4: Self-governing organizations and public goods provision	165
Table 4.5: Participation in self-governing organizations, by province	183
Table 4.6: Survey questions on the trustworthiness of grassroots officials	184
Table 4.7: Political trust index scores, by province	185
Table 4.8: Measures of local government performance	186
Table 4.9: Political distrust and participation in self-governing organizations: main model specification and hypotheses	190
Table 4.10: Results of the first-stage regression (nonrecursive model)	193
Table 4.11: 3SLS estimates of the relationship between political distrust and participation in self-governing organizations (nonrecursive model)	194
Table 4.12: 3SLS estimates of the relationship between political distrust and participation in self-governing organizations (recursive model)	195

List of Boxes and Figures

Box 2.1: Fiscal federalism theories	71
Box 2.2: The tax-for-fee reform	78
Box 4.1: The village elders' association of Liyuan (Fujian)	169
Box 4.2: The village elders' association of West Gate (Fujian)	169
Figure 2.1: Transmission of central transfers to rural areas	66

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Chapter One

Introduction

1.1 Research Objectives

Decentralization has long been viewed as a possible solution to the problems of lack of government accountability and poor service provision in developing countries. It is argued that the devolution of authority and resources to the local level can make government more accountable to citizens, by promoting local democracy and interjurisdictional competition (e.g., Bardhan and Mookherjee 2006b). At the same time, empirical evidence on the impact of decentralization on service provision shows that differences in the goals, design, implementation and context of decentralization reforms have led to different outcomes across and within countries (Crook and Manor 1998; Agrawal and Ribot 1999; Manor 1999; Olowu and Wunsch 2004; Bardhan and Mookherjee 2006a; Smoke et al. 2006; Grindle 2007; Tsai 2007b; Faguet 2012; Lu 2015). Whether by design or default, decentralization has often failed to create the “internal democratic pressures” (i.e., democratic accountability) and the “external competitive pressures” (i.e., interjurisdictional competition) required to improve local governance and service delivery (Bardhan and Mookherjee 2006b). One of the reasons is that “most decentralization efforts end up without increasing the powers of local authorities or peoples” (Agrawal and Ribot 1999: 473-474).

In recent years, China has taken “a surprising turn towards recentralization” (Oi et al. 2012: 649). Nowhere is this shift in central-local relations more evident than in the rural areas, where the central government has implemented a series of reforms aimed at: (i) eliminating agricultural taxes and fees and transferring resources to local governments through (mostly, earmarked) grants (e.g., Fock and Wong 2008); (ii) making grassroots governments more accountable to higher levels of government under the cadre responsibility system (e.g., Heberer and Trappel 2013); (iii) limiting the autonomy and decision-making power of village officials (e.g., Oi et al. 2012); (iv) reinforcing the dominant role of the Party in village governance (e.g., Alpermann 2010, 2013); and (v) promoting “intra-Party democracy”, rather than “grassroots democracy” (e.g., Brown 2011).

Whether these reforms can improve local governance¹ and public goods² provision in rural communities is an important question. The purpose of this study is to investigate how the distribution of *power* (i.e., control over fiscal resources) between levels of the Party-state, and between Party and non-Party institutions at the village level, affects patterns of *accountability* and *participation* in service delivery across rural communities. It pursues three objectives. The first one is to examine whether political decentralization, where it has occurred, has made village governments more accountable to villagers and improved their performance in providing basic infrastructure. Although villages are not considered an official level of government in China, they are regarded as “the most important level of the public sector in terms of building rural infrastructure and providing a solid fiscal foundation for the provision of rural public services” (Bird et al. 2011: 227).

A second objective of this study is to examine whether recent fiscal, administrative and political reforms have undermined the power of village committees and the meaningfulness of village-level democratic institutions, creating an “accountability gap” in service provision that cannot be filled by the Party’s mechanisms of accountability alone, whether fiscal (i.e., earmarked transfers), administrative (i.e., performance contracts) or political (i.e., intra-Party elections).

Our third objective is to investigate the interactive relationship between government performance and non-government provision of basic services. We examine whether and how the fact that villagers form their own organizations to address community needs reflects and contributes to the decline in the legitimacy of the (local) state.

¹ In line with Shah and Shah (2006: 1-2), local governance is defined as “the formulation and execution of collective action at the local level, which encompasses the direct and indirect roles of formal institutions of local government and government hierarchies, as well as the roles of informal norms, networks, community organizations, and neighbourhood associations in pursuing collective action by defining the framework for citizen-citizen and citizen-state interactions, collective decision making, and delivery of local public services”.

² The term “public goods” is used to refer to “local public goods”, that is, to “public goods whose benefits involve only a small jurisdiction” (Cornes and Sandler 1996: 32) and, in this case, villages. The terms “public goods” and “public services” are used interchangeably.

1.2 Research Questions

1.2.1 *Political Decentralization, Government Accountability, and Public Goods Provision*

In China, political decentralization reforms have only been implemented at the village level, and have been implemented unevenly across villages. Almost twenty years have passed since the enactment of the 1998 Organic Law of Village Committees and the introduction of elections in the country's more than 600,000 villages, but there are still significant differences among them in terms of how elections are conducted, and how much power is given to village committees (O'Brien and Zhao 2011). Any assessment of the degree of political decentralization in the rural Chinese context needs to consider whether those who govern rural communities are elected by and accountable to villagers. It needs to consider the procedural and substantive dimensions of village democracy: (i) the democratic quality of village elections, and (ii) the autonomy and authority of (elected) village committees vis-à-vis local Party organizations (O'Brien and Han 2009).

One of the main questions addressed in this study is whether, and under what conditions, political decentralization leads to better local governance and public goods provision in rural China. In particular, do villages that are governed by democratically elected village committees have higher levels of investment in infrastructure? Are their leaders more responsive to villagers' demands for better roads and irrigation systems or school buildings? Differences in the degree of political decentralization across villages may explain differences among them in terms of their responsiveness to the spending preferences of village residents and of their levels of investment in basic infrastructure.

To date, however, there is little consensus in the empirical literature on whether village committee elections provide an effective mechanism for village residents to hold grassroots officials accountable for the quality of the infrastructure provided in their communities (Zhang et al. 2004; Luo et al. 2007, 2010; Tsai 2007ab; Wang and Yao 2007; Sato 2008; Kung et al. 2009; Martinez-Bravo et al. 2011; Meng and Zhang 2011; Mu and Zhang 2014; Lu 2015). Some studies provide evidence of a positive relationship between elections and public goods provision and

argue that “directly elected leaders are more responsive to villager demands for public investment” (Luo et al. 2007: 599). In contrast, others raise questions about the usefulness of village elections, arguing that they are “neither necessary nor sufficient for governmental accountability and responsible provision of public goods” (Tsai 2007b: 203).

A possible limitation of existing studies, and a possible reason why they have come to such different conclusions, is that, in their analysis of the relationship between village democratic reforms and public goods provision, they focus on whether and how village committee elections are conducted, but pay little attention to what happens between elections. They fail to engage with issues of power and, in particular, to examine who has control over fiscal resources. An often implicit assumption is that spending decisions on village infrastructure are made at the village level, and are made by village committees.

However, this may often not be the case. One reason has to do with the (vertical) distribution of power between levels of government. The introduction of the tax-sharing system (1994), the implementation of the tax-for-fee reform (2002-04), and the abolition of agricultural taxes (2004-06) have “hollowed out” village finances (Fock and Wong 2008: 22). They have limited the discretionary authority of village governments to determine the level and composition of their expenditures, by reducing their revenue-raising capacity, while making them heavily dependent on (mostly, earmarked) transfers from higher-level governments (Fock and Wong 2008; Liu M. et al. 2009; Tan 2010; Bird et al. 2011; Oi et al. 2012; Boyle et al 2014). One of the consequences is that higher-level governments finance a large share of village infrastructure investment (e.g., Oi et al. 2012) and, in some cases, also implement village infrastructure projects independently (e.g., Wong et al. 2013).

Another reason why village committees may have no say in the provision of public goods has to do with the (horizontal) distribution of power between Party and non-Party institutions at the village level. The 2010 Organic Law of Village Committees has not established a clear division of competencies between village committees and village Party branches (e.g., Alpermann 2010, 2013). Indeed, by highlighting the “leading” role of Party organizations in local governance (Article

4)³, the Law places village committees in a subordinate position to village Party branches and, ultimately, to township Party committees. This implies that, even when villages can use their own funds to improve their infrastructure, it is often village Party secretaries, not village committee heads, the ones who decide whether to allocate resources for this purpose.

For these reasons, an analysis of the impact of village committee elections on public goods provision that focuses on the accountability relations between village committees and villagers, without simultaneously examining the power relations between village committees, higher-level governments and village Party organizations, might assume a greater degree of decentralization than actually exists and, consequently, fail to provide an adequate explanation for the failure of elections to improve the accountability and performance of village governments in some villages but not in others. Only if village committees are given the power to govern (i.e., control over resources), can (free and fair) elections be expected to deliver accountability⁴.

³ In Article 4 of the 2010 Organic Law of Village Committees it is stated that: “the rural organization of the Chinese Communist Party... plays a leading role in guiding and supporting the villagers’ committee’s fulfillment of duties, and supports and ensures the villagers conduct self-governance and execute their right to democracy in accordance with the Constitution and other laws”. The full text of the law is available at: www.lawinfochina.com/display.aspx?lib=law&id=8445

⁴ To our knowledge, there is no study that simultaneously considers the way in which the “vertical” and “horizontal” distribution of power – or, in other words, the interplay between the fiscal and political dimensions of the (de-)centralization process – shapes the accountability role of village elections in rural communities after the implementation of the tax-for-fee reform. The study conducted by Zhang et al. (2004) examines how the (horizontal) distribution of power at the village level affects the level and composition of village spending. They distinguish three types of villages, depending on who has the power to make spending decisions: (i) “the party secretary or village head”; (ii) “the party secretary and village head”; or (iii) “the village committee rather than individual leaders” (Zhang et al. 2004: 17). One of their main findings is that “when decisions are made by a group of people rather than by one or two individuals, the efficiency of public spending is higher” (Zhang et al. 2004: 19). The main difference between their study and ours is that their analysis focuses on whether local spending decisions are made individually or collectively, rather than on whether they are made by appointed or democratically elected officials. Unlike Zhang et al.’s (2004) study, more recent studies have examined how the (vertical) distribution of power between different levels of government affects the relationship between village elections and public goods investment at the village level after the implementation of the tax-for-fee reform (Luo et al. 2007, 2010; Zhang et al. 2007; Martinez-Bravo et al. 2011). However, they arrive at different findings and conclusions. Research by Luo et al. (2007, 2010) and Zhang et al. (2007) suggests that there is a positive relationship between village elections and all types of public goods investment at the village level, regardless of the source of investment (i.e., the village or higher levels). However, findings by Martinez-Bravo et al. (2011) show that, while there is a positive relationship between village elections and village-financed investment, there is no such relationship between elections and government-financed investment. In their view, “the effects of elections on public investment are entirely driven by increases in funding from villagers” (Martinez-Bravo et al. 2011: 22). What these studies have in common is that do not examine the possible

To gain a better understanding of the accountability role of elections in rural China after the implementation of the tax-for-fee reform, this study examines whether inter-village differences in (i) the quality of local electoral institutions and practices, and in (ii) the features of the local power structure explain variation in public goods provision across villages. Using survey data from 115 villages collected by the Center for Chinese Agricultural Policy at the Chinese Academy of Sciences, it first evaluates the democratic quality of elections across villages, by examining the three most critical aspects or stages of the electoral process: how election committees⁵ were formed in the last election – whether their members were selected by villagers or local officials; how candidates were nominated – whether they were directly nominated by voters in open primaries or through other procedures; and how votes were cast – whether secretly or publicly; whether in person or by proxy; and whether at a polling station or at roving ballot boxes.

Additionally, it examines whether the official(s) who have control over the village budget are subject to electoral control. The analysis distinguishes two types of villages. In the first type, those elected by villagers have the power to govern. This category includes: (i) villages with a “dual power structure” (Sun et al. 2013), where the elected village committee (head) plays (at least) as important a role as the village party branch (secretary) in the management of village finances; and (ii) villages with a “unitary power structure” (Sun et al. 2013), where the posts of village committee head and Party branch secretary have been merged, and where the village leader is elected by villagers in competitive elections. In the second type of villages, those who govern are not actually elected by villagers. This category includes: (i) villages with a dual power structure, where the village Party branch (secretary) has full control over village finances; and (ii) villages where the posts of village head and Party secretary are held by the same person, but (s)he is not elected through competitive elections.

The basic hypothesis is that villages that are governed by democratically elected officials may allocate more resources to the provision of public goods. More

relationship between the (horizontal) distribution of power at the village level and the amount of investment *made* or *received* by villages. Our study aims to fill this gap.

⁵ Village election committees are responsible for organizing and overseeing the electoral process.

specifically, villages where (i) elections are better implemented, and where (ii) popularly elected village committees (leaders) have control over the allocation of village funds, may invest more in infrastructure. They may allocate a larger share of the village budget to improving roads, drinking and irrigation water, and schools - the public goods most valued by villagers (Yi et al. 2011) – in order to increase their chances of re-election.

Our analysis of the impact of local democracy on local public goods provision is mainly aimed at explaining differences in the amount of public investment made by villages⁶. Recent studies suggest that, when examining the determinants of public goods investment in village communities, it is necessary to distinguish investments by the source of funding - village governments or higher-level governments. Investments decisions made by different political actors may be influenced differently by the same factors (Luo et al. 2007; Zhang et al. 2007; Boyle et al. 2014). While higher-level governments may not necessarily allocate more transfers to more democratic villages, more democratic villages may be able to mobilize more resources from villagers for infrastructure projects. The question of how village officials allocate village funds is important in light of recent evidence showing that in some villages “transfers are only replacing local expenditures rather than adding resources, as local governments divert their own resources to other uses” (World Bank 2007: 31).

⁶ In rural China, village infrastructure projects (e.g., roads, bridges, irrigation, drainage, drinking water, and schools) are typically financed either by village governments from current revenues, savings or debt, or by higher-level governments through capital grants (e.g., Luo et al. 2007, 2010; Zhang et al. 2007; Bird et al. 2011; Boyle et al. 2014). Following Park and Wang (2010) we use the terms “village-financed investment” and “government-financed investment” to refer to investment projects funded by village governments and higher-level governments, respectively. Our analysis focuses on explaining inter-village differences in village-financed investment. The question of what explains variation in government-financed investment across villages will also be explored.

1.2.2 *The Use of Transfers, Performance Contracts and Intra-Party Elections: Implications for Political Decentralization and Public Goods Provision*

Despite the need to make village governments more accountable to rural residents, the issue of political decentralization does not figure prominently in the government's strategy to "build a new socialist countryside" and to address the "three rural problems" (*san nong wenti*) of "farmers" (*nongmin*), "agriculture" (*nongye*) and "villages" (*nongcun*)⁷ (e.g., Fock and Wong 2008; Ahlers and Schubert 2009; Schubert and Ahlers 2011). To ensure accountability in the provision of rural public goods, the central government appears to have adopted a three-pronged approach: (i) transferring more resources to rural governments through earmarked grants (e.g., Luo et al. 2007, 2010; Fock and Wong 2008; Liu M. et al. 2009; Bird et al. 2011); (ii) enhancing the effectiveness of the cadre responsibility system, through the adoption of the "salary-from-above" and "cadre-in-residence" policies⁸ (e.g., Smith 2010; Oi et al. 2012); and (iii) making village Party secretaries more accountable to village Party members, through the introduction of elections for village Party branches (e.g., Guo and Bernstein 2004; Sun et al. 2013).

These reforms have had three major consequences. First, most infrastructure investment in rural communities is now financed by (earmarked) transfers from the central government, which are allocated among villages on an *ad hoc* basis by county and township governments (Luo et al. 2007, 2010; World Bank 2007; Zhang et al. 2007; Fock and Wong 2008; Bird et al. 2011; Yi et al. 2011; Oi et al. 2012; Boyle et al. 2014). Second, the salaries of the top village officials are now paid by higher-level governments rather than from village budgets (Oi et al. 2012; Chen 2015), and an "unprecedented" number of township officials works as "sent-down cadres" in villages (Smith 2010: 262). Third, the introduction of elections for village Party

⁷ The plan "to build a new socialist countryside" was approved by the National People's Congress in March 2006. As pointed out by Schubert and Ahlers (2011: 28) it represents "the Chinese state's most recent move to link its objectives of agricultural modernization, rural governance innovation, and fiscal reform in the local state". The main objectives of the plan are to promote "advanced production (*shengchan fazhan*), a comfortable livelihood (*shenhuo kuanyu*), a civilized lifestyle (*xiangfeng wenming*), clean and tidy villages (*cunrong zhengjie*), and democratic administration (*guanli minzhu*)" (Schubert and Ahlers 2011: 28).

⁸ The features of the cadre responsibility system, as well as the content of the "salaries-from-above" and "cadre-in-residence" policies will be discussed in section 1.3.4.

branch secretaries has helped to address “the democratic deficit” of grassroots Party organizations, at least in form if not in substance, and has served to reinforce their dominant position in village governance (Sun et al. 2013).

One possible concern with these fiscal, administrative, and political reforms is that, by shifting power away from village committees towards county, township and village-level Party organizations, they may undermine the effectiveness of village elections and widen the “accountability gap” in village governance – a gap that may not be filled by relying solely on the Party’s internal mechanisms of accountability. To gain a better understanding of the obstacles to, and reasons for, promoting political decentralization reforms in Chinese rural communities, this study will explore two additional questions: How does the implementation of the intergovernmental transfer system, the cadre responsibility system, and the intra-Party election system affect the power of village committees and, ultimately, the meaningfulness of village elections? And, how effective are the cadre responsibility system and the intra-Party election system in providing incentives to grassroots Party officials to invest in public goods?

The first question is related to the impact of the above mentioned reforms on the political decentralization process at the village level. In the past, county, township and village Party officials have been “the most fervent opponents” of village elections and self-government (Thornton 2008: 6). The development of “grassroots democracy” has made it more difficult for county and township Party secretaries to “manage” (elected) village cadres (Huang and Chen 2010: 52), and to elicit their cooperation in the implementation of unpopular policies (e.g., one-child policy, land acquisition, etc.) – a necessary condition for career advancement under the cadre responsibility system (e.g., O’Brien and Li 1999). They complain that the “democratic election of village cadres is not a good method, because elected cadres do not obey orders” (Li 2001: 5). The process of grassroots democratization has also made it more difficult for (appointed) village Party secretaries to maintain their position as “the undisputed boss of the village” (Guo and Bernstein 2004: 258), as they lack the democratic legitimacy that (elected) village heads often have.

By increasing their resources, authority and legitimacy, the fiscal, administrative and political reforms outlined above may provide county, township

and village-level Party committees with the means and justification to undermine the role of village committees in village governance even when – or especially when – they are democratically elected. Recent studies point in this direction (Ahlers and Schubert 2009; Sun et al. 2013). On the one hand, villages governed by democratically elected village committees appear to be less likely to receive transfers for infrastructure projects from county and township governments. Case study research shows that the political characteristics of villages - “the degree of ‘peaceful’ cooperation within a village between the village and party committees” and “the quality of communication between the cadres bureaucracies at the village, township and county levels” (Ahlers and Schubert 2009: 55) – are one of the criteria used by county and township governments to allocate grants among villages.

On the other hand, it has been found that the implementation of the cadre responsibility system and of intra-Party democratic reforms may, in some cases, result in a shift of power away from village committees to village Party branches. In particular, villages are less likely to be governed by democratically elected village committees, where: “(1) township leaders depend more heavily in village authorities for fulfilment of mandatory policy goals; and (2) selection procedures for Party branch secretaries are more representative” (Sun et al. 2013: 3).

In sum, the new fiscal, bureaucratic, and political institutions put in place by the central government to improve governance and public goods provision in rural areas may be used by local Party officials to reinforce the old power structure. This may hinder, or even reverse, the political decentralization process and thereby weaken the system of checks and balances in village governance. Following Zhang et al. (2007) and Sun et al. (2013), this study will explore: whether and how variation across villages in the degree of transfer dependence (i.e., government-financed investment)⁹, top-down Party control (i.e., the cadre responsibility system), and intra-Party democracy (i.e., intra-Party elections) is associated with variation in the degree of political decentralization (i.e., village democratic reforms). The purpose is to shed

⁹ More specifically, we will examine two issues: (i) whether county and township Party committees target transfers to villages where the Party branch remains the dominant governing body; and (ii) whether this tends to undermine demand for and support of village democratic reforms among villagers.

light on the obstacles and limits to political decentralization in the current institutional context.

Given that the balance of power between village committees and village Party branches appears to be increasingly tilted towards the latter, the second question that needs to be addressed is the extent to which township Party committees and village Party members are willing and able to hold village Party secretaries accountable for investing in community infrastructure. More specifically, how effective are the cadre responsibility system and Party elections as mechanisms of accountability?

Recent studies raise doubts about their effectiveness and suggest that they may not be sufficient to ensure accountability in rural public goods provision. For instance, according to Tsai (2007b: 232-240), the cadre responsibility system has largely failed to create incentives for village Party secretaries to improve basic infrastructure. She argues that township Party officials are unwilling and unable to hold their subordinates accountable for meeting villagers' demands for paved roads, running water infrastructure and school facilities, and points to their lack of "incentives", "leverage" and "information" as the main reasons. To our knowledge, no previous study has examined the impact of intra-Party elections on village public goods provision. However, there is evidence showing that they are less institutionalized, and more easily manipulated by township Party officials, than village committee elections (He 2007; Sun et al. 2013). According to He (2007: 119), "party elections are still exclusive; party discipline ensures the 'right' candidate is nominated by party members; the level of competitiveness is low; and township leaders still hold power to control the elected party secretaries by means of party discipline". To the extent that this is the case, they are unlikely to make village Party secretaries more accountable to village Party members for their performance. To compare the accountability effects of village committee elections (i.e., political decentralization) with those of the Party's (top-down and bottom-up) control mechanisms, this study will examine: (i) whether and how differences in the degree of accountability of village Party officials both to higher-level Party committees under the cadre responsibility system (i.e., administrative centralization), and to village Party members through Party elections (i.e., intra-Party democratization) translate into differences among villages in their investment in infrastructure. In sum,

administrative and fiscal centralization may have a negative impact on political decentralization. At the same time, fiscal and administrative control may be a poor substitute for democratic control, especially given the shortcomings of the intergovernmental transfer system and cadre responsibility system.

1.2.3 “Substitutive” Public Goods Provision by Self-Governing Organizations

Recent studies indicate that, despite the reduction of the “peasant burden” that resulted from the implementation of the rural tax reform, it has become increasingly difficult for grassroots officials to collect (legal) taxes and fees in some villages (Liu et al. 2012: 194). At the same time, it has been found that variation in the “extractive capacity” of the (local) state is associated with variation in the level of participation in “self-governing organizations” – community-based organizations that are run by villagers, not officials. Villagers are less willing to pay taxes and fees in villages where these community-based organizations have become a “substitute” for the (local) state in the provision of basic public goods: the higher the level of participation in these organizations, the lower the extractive capacity of the (local) state (Liu et al. 2012: 202).

These findings raise some fundamental questions that this study seeks to address: What explains participation in self-governing organizations? What forms do they take? To what extent are they able to substitute for the (local) state in the provision of basic infrastructure? And what implications does this have for its legitimacy and ability to govern rural communities effectively?

There is a growing body of literature on the impact of social organizations on local governance and public goods provision in rural China (Tsai 2002, 2007ab; 2011; Hansen 2008; Kung et al. 2009; Thogersen 2009; Lu 2015; Xu and Yao 2015). Most of these studies examine how traditional organizations, such as temples and lineages, are intertwined with formal Party-state institutions; how they can reinforce their legitimacy and power; and how they can improve their accountability and performance. One of their main findings is that the presence in rural communities of traditional organizations that include both villagers and officials as members allows

the former to hold the latter accountable for public goods provision through the use of social sanctions.

Of particular significance is the work of Tsai (2007ab). She proposes a “model of informal accountability” (Tsai 2007a: 356-357; Tsai 2007b: 86-119), which posits that “in political systems with weak formal institutions of accountability, localities with encompassing and embedding solidary groups are likely to have better governmental provision of public goods than localities without these groups, all other things being equal”¹⁰ (Tsai 2007b: 120). Based on a sample of more than three hundred villages from Fujian, Hebei, Jiangxi and Shanxi, her research finds that villages with temple and lineage groups (i.e., solidary groups), which are both “encompassing” (i.e., are open to everyone in the village) and “embedding” (i.e., incorporate local officials into the group as members) are more likely to have higher levels of investment in public goods, and better infrastructure. She argues that “encompassing and embedding solidary groups” can improve village public goods provision by increasing “mutual accountability between villagers and officials” (Tsai 2007b: 166). In communities with these groups, officials are more likely to feel a strong social obligation to meet villagers’ demands for public goods, which in turn makes villagers more willing to pay taxes and fees and to participate in the co-production of public goods with officials.

Like these studies, we investigate the interaction between informal and formal institutions in the context of public goods provision in rural China¹¹. However, our research differs from theirs in three ways. The first difference lies in the types of organizations studied. Self-governing organizations have two distinctive features: (i) they are run neither by local officials nor by their appointees but by villagers, and (ii) they do not incorporate local officials in their activities or decision-making processes. Two distinctions can be made between what we call “self-governing organizations”

¹⁰ Solidary groups are defined as “collections of individuals engaged in mutually oriented activities who share a set of ethical standards and moral obligations” (Tsai 2007a: 356; Tsai 2007b: 4). Examples include temples, churches and lineages. These groups are “encompassing” when they are “open to everyone under the local government’s jurisdiction”, and “embedding” when they “incorporate local officials into the groups as members” (Tsai 2007a: 356; Tsai 2007b: 13).

¹¹ Institutions are defined as “the rules of the game” or the “humanly devised constraints that shape human interaction” (North 1990: 3). We use a “state-societal distinction” to distinguish between “formal” and “informal” institutions (Helmke and Levitsky 2004: 727).

and what Tsai (2007ab) calls “encompassing and embedding solidary groups”. First, not all self-governing organizations are “solidary groups”. Our analysis is not confined to groups based on “shared moral obligations and ethical standards” (Tsai 2007b: 94), but instead includes other types of community organizations, such as farmers’ cooperatives or cultural associations. Second, although some types of self-governing organizations, such as Christian churches or the so-called financial management small groups (*licai xiaozu*)¹², can be regarded as “solidary groups”, they are not both “encompassing” and “embedding”. They may be “encompassing” (i.e., open for participation to all villagers), but not “embedding” (i.e., open to Party and government officials).

A second difference between these studies and ours is the forms of public goods provision examined. The presence of “encompassing and embedding solidary groups” in village communities has been found to have a positive impact on the state’s provision of infrastructure (Tsai 2007ab). By enabling villagers to use social sanctions against corrupt village officials, these groups can help overcome “the accountability problem” associated with the *governmental provision of public goods* (Tsai 2007ab). Unlike these groups, self-governing organizations lack leverage over local officials and, consequently, may be unable to hold them accountable for their investment in infrastructure. However, their presence in village communities may have a positive effect on the level of non-state provision of public goods. Some of these organizations may be able to raise voluntary contributions from villagers and to provide the goods and services that are under-provided by the state. They may help villagers overcome the “collective action problem” associated with the *non-governmental provision of public goods*¹³, by fostering cooperation among them and preventing free-riding problems.

A third difference between our research and previous studies (Tsai 2007ab; Lu 2015; Xu and Yao 2015) is related to the direction of the causal relationship between community participation and (local) state performance. While the main objective of

¹² The members of these groups are elected by and among villagers and are responsible for monitoring the use of village funds (Su and Yang 2005: 144).

¹³ The literature on social capital suggests that participation in these organizations may reduce the free-riding problem (i) by fostering “norms of reciprocity” among their members; (ii) by generating “information” about their behaviour; (iii) and by imposing “social sanctions” against free-riders (Putnam 1993: 174).

these studies is to investigate how the presence of community organizations may (positively) affect the performance of local governments (e.g., Tsai 2007ab; Lu 2015; Xu and Yao 2015), we examine the interactive relationship between both variables, but emphasize the opposite direction of their causal relationship, that is, how the quality of local government affects the types of organizations villagers join and contribute time and money to. While these studies argue that the key to good governance in rural China lies in having “the right kind of organizations” i.e., those that bring villagers and officials together (Tsai 2007b: 247), our study asks whether we can have the right kind of organizations without having the “right” kind of government.

The point of departure for our analysis of the emergence and impact of self-governing organizations in Chinese rural communities is the idea that, in the context of public goods provision, the relationship between state and non-state actors – whether one of complementarity or substitution - *reflects* and *affects* state legitimacy and capacity (Evans 1996; Narayan 1999; Ostrom 1996; Woolcock and Narayan 2000; Robinson and White 2001; Joshi and Moore 2004; Cammet and MacLean 2011; McLoughlin 2011; Tsai 2011; Batley et al. 2012; Bodea and Lebas 2014).

When state institutions are strong, non-state provision is more likely to take the form of co-production than self-provision¹⁴: non-state actors are more likely to provide public goods in collaboration with, rather than independently of, state agencies. This in turn may have a positive impact on the quality of state-society relations and, ultimately, on the level of state capacity (e.g., Evans 1996; Ostrom 1996; Robinson and White 2001; Tsai 2011). On the other hand, where state institutions fail to meet demands for public goods and are perceived with distrust, non-state organizations may emerge to fill the gap in governance. Yet, at the same time, the fact that they replace the state in the provision of basic services may further undermine the legitimacy and performance of state institutions (e.g., Narayan 1999; Woolcock and Narayan 2000; Bodea and Lebas 2014).

¹⁴ In rural China, two main types of non-state provision of public goods can be distinguished: “*substitutive* provision” by non-state actors and “*co-production*” between state and non-state actors (Tsai 2011: 48). The main difference lies in whether non-state actors provide public goods in collaboration with state agencies or independently (Joshi and Moore 2004: 31; Tsai 2011: 48-49).

There is evidence of the growth of “autonomous” non-state organizations (Watson 2008) and “substitutive” public goods provision (Tsai 2011) in rural China, yet little understanding of the determinants and outcomes of these forms of collective action. Using survey data collected by the the Center for Chinese Agricultural Policy on more than 500 village organizations – including, old people’s associations, wedding and funeral councils, Buddhist temples and Christian churches, mutual aid groups, and others -, this study aims to shed light on these two issues. A first aim is to explain what determines villagers’ incentives and capacity to form their own organizations and to provide themselves with public goods. To this end, we examine whether variation across villages in the level of participation in self-governing organizations is explained by variation in: (i) the level of trust between villagers and township officials; (ii) the amount of investment in village infrastructure; and (iii) the quality of village committee elections. Additionally, we examine how clan structure and rural-urban migration processes constrain or enable the development of these organizations.

A second aim is to explore the limits and possible consequences of villagers’ involvement in self-governing organizations and non-state provision of public goods in rural China. To assess the service provision role of non-state organizations, we examine the involvement of self-governing organizations in the construction and maintenance of village roads and bridges, drinking water and irrigations systems, and primary school buildings – the public goods that villagers care most about (Yi et al. 2011). Additionally, to explore the effects of non-state organizations and non-state provision on (local) state legitimacy and capacity, we examine whether there is a feedback effect between participation in self-governing organizations and trust in township officials: participation in these organizations may not only reflect but also contribute to the declining legitimacy of township governments. Given the lack of institutionalized channels through which higher levels of political distrust can translate into higher levels of government accountability and performance at the township level (e.g., electoral accountability), an increase in political distrust is likely to have a negative impact on the capacity of local officials to govern effectively, whether through a reduction in compliance with state policies (e.g., taxation) or

through an increase in non-institutionalized forms of political participation (e.g., social protests).

The basic hypothesis is that the emergence of self-governing organizations in rural areas may be more a symptom than a solution to the problems of poor local governance and inadequate public goods provision. As a result of recent recentralization reforms, township officials can exercise an unprecedented degree of control over village governance – how villages are governed and by whom. However, they are neither elected by nor accountable to villagers. In communities where the legitimacy of (higher-level) state actors is low, and the performance of state institutions poor, villagers may have strong incentives to form their own organizations, and to provide themselves with the goods and services that are not provided by the state. At the same time, the social capital and collective action literatures suggest that their ability to do so may depend on their community's social and economic characteristics and, especially, on whether clan ties foster integration within the village and on whether migration networks provide access to resources outside the village (e.g., Woolcock 1998; Narayan 1999; Ostrom and Ahn 2001). Hence, self-governing organizations may be able to meet the infrastructure needs that are left unmet by local governments in some villages but not in others. As “substitutive informal institutions”, they are likely to be only a “second-best solution” (Helmke and Levitsky 2004) to the problem of underprovision of local public goods in villages where formal institutions in general, and elections in particular, fail to provide a mechanism for holding accountable those who actually govern them¹⁵.

¹⁵ Helmke and Levitsky (2004: 729-730) point out that “substitutive informal institutions” tend to emerge where formal institutions are “weak or lack authority”. In their view, they are a ‘second best’ strategy for actors who lack the power to change the way formal institutions function.

1.3 Background

1.3.1 *(De-)centralization in Rural China: Power, Accountability and Participation*

Since the late 1980s, and especially after the enactment of the revised Organic Law of Village Committees in 1998, China has carried out political decentralization reforms at the village level with the objective of making village governments more accountable to villagers. The introduction of elections for village committees and the creation of village (representative) assemblies and village affairs control groups have provided new mechanisms for villagers to hold village committees accountable for the provision of public goods (Choate 1997; Kelliher 1997; O'Brien and Li 2000; Pastor and Tan 2000; Alpermann 2001, 2010, 2013; O'Brien and Zhao 2011; Schubert and Ahlers 2012a). However, at the same time, there is evidence that the distribution of resources and decision-making power in rural China is increasingly skewed towards county, township and village-level Party committees (e.g., He 2007; Oi et al. 2012; Schubert and Ahlers 2012a; Sun et al. 2013; Chen 2015). For instance, a recent study based on a sample of eighty villages from eight provinces shows that the position of the Party secretary in village governance “remains dominant in nearly all villages – even in those where elections are largely free and fair” (Chen 2015: 13). This suggests the existence of what, for lack of a better term, might be called the “accountability-power paradox” in village governance: villagers have the mechanisms to hold village committees accountable but village committees do not have the power to govern.

In the remainder of this section, we discuss some of the possible causes and consequences of this paradox. We examine the political, fiscal, administrative and institutional aspects of (de-)centralization at the village level with two objectives. The first one is to outline some of the factors underlying the distribution of power between levels of government, and between Party and non-Party institutions at the village level, including the lack of a clear legal framework for village governance, the centralization of the fiscal and administrative systems and the introduction of elections for village Party branches. The second one is to discuss current trends in local governance, with a particular focus on issues of accountability and participation. Two points are made. First, recent changes in the local governance

system – changes aimed at increasing the resources, authority and legitimacy of Party organizations at various levels - may have the effect of undermining the power of village committees and, consequently, the ability of villagers to hold local officials accountable for the provision of public goods through elections and other democratic institutions. This may create an “accountability gap” in village governance that cannot be filled by other accountability mechanisms – whether fiscal (e.g., earmarked transfers), administrative (e.g., performance contracts) or political (e.g., intra-Party elections). Second, in many parts of rural China, state-society relations may be characterized, neither by cooperation nor by conflict, but by disengagement. This may weaken the incentives of villagers to participate in community organizations with close ties to the state, as well as in the co-production of public goods with officials.

1.3.2 Village Elections

The 1987, 1998, and 2010 Organic Laws of Village Committees have provided the legal basis for the gradual implementation of political decentralization reforms in Chinese villages¹⁶ (Choate 1997; Kelliher 1997; O’Brien and Li 2000; Pastor and Tan 2000; Alpermann 2001, 2010, 2013; O’Brien and Zhao 2011; Schubert and Ahlers 2012a). In the three versions of the Organic Law, village committees are defined as a “mass organization of self-government”, whose members must be directly elected by villagers every three years (without term limits), and whose primary functions are to “manage the public affairs and public welfare

¹⁶ Village committees emerged spontaneously in two Guangxi counties in the early 1980s. They were established by villagers in order to provide for basic community needs and to fill the vacuum of governance left by the gradual dismantlement of the People’s Commune system. Their members were elected by villagers and their role was limited to managing community affairs, such as the construction and maintenance of community infrastructure (Choate 1997: 5; O’Brien and Li 2000: 465-466). The 1982 Constitution gave village committees legal recognition as “elected, mass organizations of self-government” (Article 111) and by the end of 1984 around 700,000 brigades had been replaced by nearly 950,000 village committees (O’Brien and Li 2000: 467; 472). It was not until 1987, after years of continued debate and negotiation between advocates and opponents of village self-government, that the National People’s Congress passed the Organic Law of Village Committees (Trial Implementation). New versions of the Organic Law were passed in 1998 and 2010 (Alpermann 2010, 2013).

undertakings of the village, mediate disputes among villagers, help maintain the public order, and convey villagers' opinions and demands and make suggestions to the people's government" (Schubert and Ahlers 2012a: 193).

Each version of the Organic Law has provided more – and seemingly more effective – channels for villagers to monitor and hold village committees accountable (Pastor and Tan 2000; Alpermann 2010, 2013; O'Brien and Zhao 2011; Schubert and Ahlers 2012a):

- Village elections, which were initially implemented on a trial basis (1987-1998), are now regularly held in the country's more than half million villages and involve more than six hundred million voters.
- Electoral procedures have been standardized and improved. The revised versions of the Organic Law include electoral rules covering each of the key stages of the electoral process: election management, voter registration, candidate nomination, campaigning, voting and vote count. In the 2010 Law¹⁷, new rules mandate that election committee members be selected at the village (representative) assembly (Art. 12), that election candidates be nominated by villagers (Art. 14), and that the election be conducted by secret ballot (Art. 15). New provisions also limit the use of proxy voting and roving ballot boxes (Art. 15).
- A new "system of open administration of village affairs" has been adopted and, for the first time, village committees are required to disclose all expenditures once every quarter (Art. 30).
- The oversight role of village (representative) assemblies, to which village committees report and are accountable (Art. 2), has been strengthened. They have been given the right to modify or cancel any "inappropriate" decision made by village committees (Art. 23).
- The deliberative role of village (representative) assemblies has also been strengthened. They have been empowered to participate in decisions about "proposals for developing public welfare undertakings, raising funds, gathering labor forces and contracting construction projects in the village" (Art. 24).

¹⁷ The full text of the 2010 Organic Law can be found in Schubert and Ahlers (2012a: 185-204) and at www.lawinfochina.com/display.aspx?lib=law&id=8445.

- Citizen monitoring groups – the so-called “village affairs supervisory committees” – have been created in each village to monitor the performance of village committees. Their members must be elected from and by villagers and must be people with “expertise in finance and management” (Art. 32).
- A “democratic” appraisal of the performance of village committee members must now be conducted by village affairs control groups once a year. Where members of the village committee are deemed “incompetent” in two consecutive years, they can be removed from office (Art. 33).
- Procedures for recalling elected officials have been simplified (Art. 16), making it easier for villagers to oust corrupt officials between elections.

As Alpermann (2013: 160) has pointed out, the 2010 Organic Law of Village Committees provides the means to strengthen the accountability of elected village officials to village voters. However, it does not provide the means to ensure that villages are actually governed by democratically elected village committees. In the 1987, 1998 and 2010 versions of the Law, there is ambiguity regarding the division of power and functions between village committees, on the one hand, and township and village Party organizations, on the other. The most recent version of the Law, like the previous ones, requires village committees to “assist” township governments in the performance of their duties (Art. 5) and establishes village Party organizations as the “leading core” in village governance (Art. 4). The failure to establish a clear framework for village governance that effectively empowers village committees vis-à-vis other political actors may ultimately render village elections, village (representative) assemblies, and village affairs monitoring groups meaningless as accountability mechanisms.

1.3.3 Fiscal Centralization

The recentralization of the fiscal system, the growth of vertical fiscal imbalances, and the resulting dependence of local governments on central transfers are the most important changes in China's local public finance in recent years (Zhang 1999; Wong 2000, 2007ab, 2009; Martinez-Vazquez 2006; Lou 2008; Wong and Bird 2008; Bahl 2011; Man 2011).

Since the mid-1990s the central government has implemented a series of fiscal reforms that have fundamentally changed how rural governments are financed. The introduction of the tax-sharing system (1994), the subsequent centralization of (enterprise and individual) income taxes (2002-03), the elimination of rural fees (2002-04) and agricultural taxes (2004-06) and the increase of transfers to rural governments under the "New Socialist Countryside" policy (2006-present) have eroded the revenue-raising capacity of rural governments, while increasing their dependence on (mostly, earmarked) transfers from the central and provincial governments to finance the provision of infrastructure and services (World Bank 2007; Fock and Wong 2008; Tian 2009; Takeuchi 2014; Chen 2015). For instance, findings from a survey of 100 villages in five provinces show that in 1997 (earmarked) transfers financed about 45 percent of investment in village-level infrastructure, while in 2008 they financed almost 75 percent (Oi et al. 2012).

Fiscal recentralization policies have sharply reduced the amount of resources over which village governments have control or discretion, limiting the scope of what they can do and be held accountable for. These policies may have limited the potential of political decentralization reforms to improve rural public goods provision and, at the same time, may have left the problem of political accountability unsolved. First, by shifting resources and decision-making power away from villages and towards counties and townships, fiscal recentralization reforms may have undermined the role of village elections as mechanisms of accountability. This is for two interrelated reasons. The first and obvious one is that county and township officials, who are not elected by villagers but appointed by higher-level Party committees, are now responsible for financing and implementing a large and growing share of village infrastructure projects (e.g., Wong et al. 2013). The second reason is related to the possible influence of political factors on the distribution of investments

across villages. Like in other countries (e.g., Khemani 2007ab; Leiderer 2014), the intergovernmental transfer system in China leaves room for a “politically motivated” distribution of resources across localities: in the rural Chinese context, county and township Party committees may target more investment to villages that are governed by Party branches rather than by popularly elected village committees. In any case, regardless of the reason, the fact that (i) most rural infrastructure investment is financed by (earmarked) transfers from the central and provincial governments, (ii) and that transfers are allocated to villages on an *ad hoc* basis by counties and townships, implies that the positive relationship between grassroots democracy and public goods provision – if and where it existed - may have disappeared or been reversed.

Second, while the central government’s increased reliance on earmarked transfers to finance rural public goods provision may have undermined the effectiveness of elections, earmarked transfers may be a poor substitute for elections as accountability mechanisms¹⁸. Existing evidence suggests that the central government has little control over how earmarked grants are actually distributed and spent by rural officials (World Bank 2007; Fock and Wong 2008; Liu M. et al. 2009; Takeuchi 2014), mainly due to the poor design and implementation of the intergovernmental transfer system, which remains “the least transparent area in China’s fiscal system” (Qiao and Shah 2006: 159). By 2020 the Chinese central government will have spent around 180 trillion yuan on the implementation of the “new socialist countryside” policy (Schubert and Ahlers 2011: 29), but a recent World Bank study reports that, as yet, “there is no centralized monitoring and evaluation system that allows the central government to comprehensively assess the overall programs; in which counties, townships and villages they are implemented; and their efficiency and impact” (Fock and Wong 2008: 43).

¹⁸ In their analysis of earmarked grants as a means to increase government accountability, Bird and Smart (2009: 18) argue that “one advantage of enforcing such controls through grant policy is that the built-in reporting back to the center of how grant funds are spent may make it easier to monitor how local governments actually do”. This is not, however, the case in China.

1.3.4 Administrative Centralization

In recent years, various administrative reforms have been implemented to enhance the effectiveness of the cadre responsibility system in rural areas, which are seen as “a decisive turn towards more centralized administrative control of townships and villages” (Oi et al. 2012: 651). The cadre responsibility system is the mechanism by which the Party monitors and holds local officials to account¹⁹. Under this system, Party committees at each level of the administrative hierarchy (e.g., township Party committees) use annual performance contracts to assign a variety of targets to lower-level officials (e.g., village Party secretaries and village heads) and to hold them accountable for fulfilling them (Whiting 2001, 2006; Edin 2003ab; Burns 2004; Tsui and Wang 2004; Heimer 2006; Kennedy 2007b; Tsai 2007b; Landry 2008; Gao 2009; Ong 2012; Birney 2014).

To make village officials more accountable to their Party superiors under the cadre responsibility system, the central government has adopted the so-called “salaries-from-above” and “cadre-in-residence” policies (Oi et al. 2012; Smith 2010). The first policy requires that the salaries of the top village officials be paid by county governments from funds transferred by the central government (Oi et al. 2012: 657). The second policy requires that (at least) one township official works as a “sent-down cadre” in each village (Smith 2010: 613-615). The objective of these policies is to reduce agency problems between village officials and county/township cadres, by providing the latter with new means to incentivize and monitor the performance of the former. Findings from a nationally representative survey of 100 villages in five provinces suggest that, by 2005, the “salaries-from-above” and “cadre-in-residence” policies had been implemented in 91 and 71 percent of China’s villages, respectively (Oi et al. 2012). While these administrative reforms may make village officials more accountable to higher-level Party cadres, it is not clear whether they can make them more accountable to villagers.

¹⁹ The cadre responsibility system is based on the nomenklatura system, which is “a list of leading positions over whose appointments the party exercises full control. Party committees exercise authority over the appointment of senior personnel, as well as promotion, dismissal and transfer one step down the administrative hierarchy” (Heimer 2006: 124).

An increase in administrative centralization may lead to a decrease in political decentralization²⁰ and, at the same time, tighter bureaucratic control over village officials may not improve public goods provision, unless performance contracts with rural officials at all levels (i.e., county, township and village) include and prioritize performance targets related to social development and grassroots political reform. Existing research suggests that the degree of administrative centralization varies across rural jurisdictions (Sun et al. 2013; Tsai 2007b), and that greater reliance on the cadre responsibility system to govern rural areas creates negative incentives for township officials to block grassroots democratic reforms, while failing to create positive incentives for them to hold village officials accountable for providing better infrastructure and services²¹. This suggests that, by reducing the decision-making power and autonomy of village committees, mechanisms of top-down control may undermine the ability of villagers to use elections as a way of providing incentives to those who govern to meet their needs. At the same time, administrative institutions, like fiscal institutions, may not be enough on their own to enhance the accountability of rural officials and to improve the provision of public goods.

²⁰ For a general discussion on the possible interrelations among the fiscal, administrative and political dimensions of decentralization see Schneider (2003).

²¹ Research by Sun et al. (2013: 17) has found that “Party branch secretaries are more likely to maintain their predominant positions in villages where township authorities are more dependent on village leaders for the implementation of policy measures”²¹. Tsai’s (2007b: 234) research, in turn, shows that the reason why greater bureaucratic control does not translate into better rural service provision is because “all performance contracts signed by officials at the township level and above prioritize economic development, industrialization and revenue generation, not the provision of public goods and services”.

1.3.5 Intra-Party Elections

Since the early 2000s, the central government has promoted “intra-Party democracy” in rural communities, through the introduction of “intra-Party elections” and a new system of “concurrent office-holding”²² (e.g., Chan 2003, 2007; Schubert 2003; Guo and Bernstein 2004; He 2007; O’Brien and Han 2009; Huang and Chen 2010; Brown 2011; Alpermann 2013; Sun et al. 2013). In some villages, Party branch secretaries are no longer appointed by the township but elected by and among village Party members. In other villages, the “dual power structure” of village committee head and Party secretary has been replaced by a “unitary power structure”, where the same person serves as both village head and Party branch secretary (Sun et al. 2013).

The implementation of these reforms is seen as part of the Party’s intention “to re-concentrate its power in rural areas” (Chan 2003: 192). However, little is known about their impact on local governance and public goods provision. To date, we know that villages where Party secretaries are elected by Party members are more likely to be governed by the Party branch rather than by the village committee (Sun et al. 2013). However, we do not know whether intra-Party democratic reforms are effective in creating incentives for them to improve the provision of public goods.

1.3.6 Participation in Local Governance

China differs from most decentralized countries in that the level of dissatisfaction with and distrust of government increases “as government gets closer to the people” (Saich 2007: 5). This is especially the case in rural areas. There is evidence that villagers distrust local officials (Li 2004, 2008); that they view grassroots governments as “useless” (Oi and Zhao 2007: 95); and that they dismiss village elections as mere “political shows” (Tao et al. 2011: 109). One of the most important consequences of the growing cleavage between villagers and local officials is the decline in various forms of participation. For instance, there is evidence that

²² In July 2002, the Central Committee and the State Council issued a circular (Document no. 14) which recommended the adoption of direct elections for village Party secretaries and encouraged merging the posts of village committee head and village Party secretary (*yijiantiao*) (Guo and Bernstein 2004; He 2007; Huang and Chen 2010; O’Brien and Han 2009).

grassroots governments are often unable to raise voluntary contributions from villagers for infrastructure projects under the so-called “one-issue-one-discussion” (*yi shi yi yi*) system²³, especially in communities where confidence in grassroots officials has been eroded by problems of corruption (e.g. Chen 2008, 2014, 2015; Fock and Wong 2008; Li 2009; Tian 2009; Göbel 2010; Boyle et al. 2014). There is also evidence that in villages where distrust of township officials is high, and where democratic institutions do not provide opportunities for meaningful participation in village affairs, villagers neither vote in elections (Tao et al. 2011) nor attend village assembly meetings (Schubert and Ahlers 2012a). Recent changes in China’s (de-)centralization policies may have created new challenges for improving cadre-villager relations in rural areas. According to Chen (2015: 259), “cadre-villager disengagement seems to be a general trend across rural China” after the implementation of the tax-for-fee reform and the abolition of agricultural taxes.

1.4 Methodology and Structure of the Thesis

To address the research questions discussed in section 1.2, this research relies on cross-sectional survey data from 115 villages collected by the Center for Chinese Agricultural Policy (Chinese Academy of Sciences) in the summer of 2005. To investigate why some village governments provide more public goods than others, we specify and estimate a simultaneous equations model²⁴, in which “village democracy” and “village public goods provision” (i.e., village-financed investment) are the endogenous variables. This has two advantages. The first one is that it allows us to address potential problems of simultaneity and endogeneity. There may be reverse causality between village democracy and village-financed investment. In villages governed by democratically elected village committees, village heads might have stronger incentives to allocate a larger share of the village budget to the provision of public goods in order to remain in office. At the same time, villagers

²³ According to the “one-issue-one-discussion” (*yishiyiyi*) system, “any fee levied must be earmarked for a specific project and collected with the consent of villagers” (Chen 2015: 181).

²⁴ The simultaneous equations models are nonrecursive unless stated otherwise.

might have stronger incentives to participate in village politics in order to monitor and influence how village funds are spent and what public goods are provided. In other words, village democracy may affect and be affected by village public goods provision, through the channels of political accountability and political participation, respectively. Given the possible interdependence between the fiscal behaviour of village leaders and the political behaviour of villagers, the use of a single-equation regression model and of the ordinary least squares estimation procedure would lead to biased and inconsistent estimates of the effects of village democracy on public goods provision (Wooldridge 2006; Gujarati and Porter 2010). A second advantage of using this model is that it allows us to include measures of the implementation of the cadre responsibility system and Party elections as exogenous variables in each of the equations and thus to examine their impact on both village democracy and village-financed investment. The assumption that these variables are exogenous to the system seems reasonable, given that decisions regarding the method for (s)electing village Party secretaries and the criteria for evaluating their performance under the cadre responsibility system are typically made by county and township leaders.

Additionally, we estimate a simultaneous equations model in which “village democracy” and “government-financed investment” are the endogenous variables. In this case, we use the share of infrastructure investment financed by transfers from higher-level governments (i.e., government-financed investment) as the main dependent variable. This will allow us to explore two questions: (i) whether county and township Party committees target transfers to villages where the Party branch remains the dominant governing body; and (ii) whether this tends to undermine the demand for and implementation of grassroots democratic reforms.

To investigate the interactive relationship between government performance and non-government provision of public goods, we develop a simultaneous equations model, with “political trust” and “participation in self-governing organizations” as the endogenous variables. In this case, the main question we seek to investigate is whether the fact that villagers form their own organizations to provide themselves with public goods reflects and contributes to the decline in satisfaction with and trust

in government in rural areas²⁵. The key exogenous variables included in the model are a village's clan structure and level of out-migration. Descriptive analysis of survey data on more than 500 community organizations is used to determine the nature of self-governing organizations and their degree of involvement in the construction and maintenance of roads, bridges, drinking water and irrigation systems, as well as school buildings.

This study consists of five chapters including the introduction and conclusion. Chapter 2 "*China's Intergovernmental Fiscal Reforms and Rural Public Finance*" pursues four objectives: (i) to analyze the processes of decentralization and recentralization that have shaped central-local fiscal relations under the fiscal contracting system (1980-1993) and the tax-sharing system (1994-present); (ii) to assess whether the intergovernmental fiscal system and interjurisdictional competition have provided rural governments with adequate (fiscal) resources and incentives to respond to local demands for public goods; (iii) to analyze China's recent rural fiscal reforms, including the implementation of the tax-for-fee reform and the abolition of agricultural taxes; and, last, (iv) to engage with a recent strand of the second-generation fiscal federalism literature – "partial decentralization" theory – (e.g., Khemani 2005; Ahmad and Brosio 2009; Devarajan et al. 2009), and to raise the question of whether decentralization at the village level has become "partial", a situation where "political and fiscal institutions are not able to ensure accountability of local elected politicians and officials" (Ahmad and Brosio 2009: 5).

Chapter 3 "*Political Institutions and the Provision of Local Public Goods*" investigates whether inter-village differences in infrastructure spending reflect inter-village differences in their governance systems, and in what ways. The focus of the analysis is on the accountability of village governments to villagers and, in particular, on how the distribution of power (i.e. control over fiscal resources) between levels of government, and between Party and non-Party institutions at the village level, affects the ability of rural residents to hold village officials to account for providing

²⁵ There is a possibility that there is a one-way relationship between political trust and participation in self-governing organizations. Political trust may influence participation in self-governing organizations, but participation in these organizations may have no impact on the political attitudes of their members. For this reason, we also develop a recursive simultaneous equations model and estimate it using three-stage least squares.

public goods. The chapter examines empirically: (i) whether variation in political decentralization across villages explains variation in their investment in infrastructure (i.e., village-financed investment); (ii) whether and how variation across villages in the degree of transfer dependence (i.e., government-financed investment), top-down Party control (i.e., the cadre responsibility system), and intra-Party democracy (i.e., intra-Party elections) is associated with variation in the degree of political decentralization (i.e., village democratic reforms)²⁶; and (iii) whether and how variation across villages in the degree of top-down Party control, and intra-Party democracy is associated with variation in the level of village-financed investment in infrastructure.

Chapter 4 “*Social Institutions and Local Public Goods Provision*” investigates how – and how effectively – village residents respond to problems of poor local governance and inadequate public goods provision. It investigates what determines villagers’ willingness and capacity to form their own organizations and provide themselves with public goods, by examining whether variation across villages in the level of participation in self-governing organizations is explained by variation in: (i) the level of trust between villagers and township officials; (ii) the amount of investment in village infrastructure; (iii) the quality of village elections; and (iv) features of the social and economic structure, namely, lineage institutions and rural-urban migration. Additionally, the chapter examines (i) the degree of involvement of self-governing organizations in the construction and maintenance of basic infrastructure, and (ii) the effects of these organizations on political trust and legitimacy.

²⁶ The underlying question was: (i) whether the cadre responsibility system creates perverse incentives for township officials to obstruct village democratic reforms; (ii) whether the intergovernmental transfer system leaves room for county and township governments to target more resources to politically favoured villages, namely, those where the village Party branch remains the dominant governing body; and (iii) whether the implementation of intra-Party democratic reforms justifies or legitimizes the lack of progress in the implementation of village democratic reforms. In other words, the use of performance contracts, intergovernmental transfers and intra-Party elections as mechanisms of accountability in rural governance may subvert rather than reinforce village democratic institutions.

1.5 The Data Set

The data set used in this study is from a survey of 115 villages conducted by the Center for Chinese Agricultural Policy (CCAP) of the Chinese Academy of Sciences in the summer of 2005 (henceforth, CCAP village survey). Stratified sampling was used to select the sample villages. The country was first divided into six regions and one province was randomly selected from each of the regions: Jilin (Northeast), Hebei (North), Shaanxi (Central), Jiangsu (East), Fujian (Southeast), and Sichuan (Southwest). All counties in each province were then ranked into quintiles according to their per capita gross value of industrial output, and one county was randomly selected from each quintile. Within each county, two townships were randomly selected from among those with per capita income above and below the median, respectively. Finally, following the same procedure, two villages were randomly selected from each township, resulting in a sample of 120 villages. Fourteen villagers and between two and four officials were randomly selected in each village. Due to unexpected difficulties (e.g., bad weather) five villages had to be dropped from the final sample. The survey covered 378 cadres and 1,550 villagers in 115 villages. It collected information about public goods provision; village finances; village democratic reforms; the relationship between villages and townships; the relationship between village committees and Party branches; villagers' political attitudes and participation; the nature and role of community organizations; and the economic, social, demographic and geographic characteristics of the sample villages. The data were collected for the years 2000 and 2004²⁷.

²⁷ The fiscal data were collected for the period 2000-2004.

1.6 Key Findings and Implications of the Study

The findings of this study shed light on how the distribution of *power* (i.e., control over fiscal resources) between levels of the Party-state apparatus, and between Party and non-Party institutions at each level, affects patterns of *accountability* and *participation* in service delivery across villages. They can be summarized as follows.

- 1) Villages where (i) elections are better implemented, and where (ii) popularly elected village committees have a say in the allocation of village funds, tend to invest more in infrastructure (i.e., village-financed investment). However, village committees are often powerless. The main challenge for increasing accountability in the provision of public goods in rural communities is not – or not only – whether voters can exercise control over elected officials (i.e., quality of village democratic institutions) but, more fundamentally, whether village committees can gain control over fiscal resources (i.e., power of village committees).
- 2) County and township Party committees tend to allocate a smaller share of (earmarked) transfers to villages that are governed by democratically elected village committees, regardless of fiscal capacity or expenditure needs considerations (i.e., government-financed investment). At the same time, villages that fund a larger share of their expenditures with transfers are more likely to be governed by Party secretaries. While more research is needed, these findings suggest that the intergovernmental transfer system provides a mechanism for higher-level Party officials to target resources to villages where power remains concentrated in the hands of their subordinates, and that this tends to undermine the implementation of grassroots political reforms.

- 3) The cadre responsibility system and intra-Party elections appear to have diametrically opposed effects on local democracy and local public goods provision at the village level. Tighter bureaucratic control over villages is not positively associated with local public goods provision (i.e., village-financed investment), but it is negatively associated with local democracy. Village governments that are less autonomous from township governments are less likely to be run by popularly elected officials, while they are not more likely to invest in public goods. In contrast, the election of village Party secretaries by village Party members (without the interference of township officials) has a significant positive impact on local public goods provision and does not have a significant negative impact on local democracy.
- 4) In villages where the legitimacy of (higher-level) state actors is low (i.e., trust in township officials), and the performance of state institutions poor (i.e., village-financed investment), villagers have strong incentives to form their own organizations, and to provide themselves with the goods and services that are not provided by the state. At the same time, their ability to do so depends on their community's social and economic characteristics and, in particular, on whether clan ties foster cohesion within the village and on whether migration networks provide access to resources outside the village.
- 5) The fact that villagers form their own organizations to address community needs represents only a "second-best solution" to the problem of under-provision of public goods in communities where formal institutions, such as elections and village representative assemblies, fail to provide a mechanism for holding accountable those who actually govern them (e.g., township officials). Increasing participation in these organizations is not only a consequence but also a cause of the declining legitimacy of the (local) state.

This study's findings have implications for the design and implementation of (de-)centralization policies in China. Two main conclusions can be drawn from them. The first one is related to the conflict between the political, fiscal, and administrative dimensions of (de-)centralization and the negative impact this has on the quality of local governance and public goods provision at the village level. Our findings suggest the following: (i) political decentralization has a positive impact on the performance of village governments in providing public goods; (ii) the processes of political decentralization and intra-Party democratization can complement one another in making village officials more (downwardly) accountable to villagers and Party members for the use of village funds; (iii) fiscal and administrative centralization have a negative impact on political decentralization and compromise its benefits, mainly by reducing the resources and autonomy of village committees; (iv) intergovernmental fiscal and administrative institutions are a poor substitute for local elections as accountability mechanisms, given the lack of transparency and objective criteria in the distribution of (earmarked) transfers among villages (i.e. government financed investment); and the failure of the cadre responsibility system to create incentives for village officials to invest in public goods (i.e., village-financed investment). While further research is needed, our study suggests that, by reducing the power of village committees, the centralization of the fiscal and administrative systems is leading to a reversal of political decentralization and to a widening of the "accountability gap" between villagers and officials.

A second conclusion is related to how the (de-)centralized system shapes the interaction between state and non-state actors in local governance. In villages where the (local) state fails to meet demands for public services, and where township officials are seen as part of the problem rather than as part of the solution, community organizations may emerge to fill the void left by state institutions. However, the fact that they replace local officials in mobilizing resources from villagers and providing services further reduces the legitimacy of the (local) state, while increasing the transaction costs of governing. This finding is consistent with recent research showing that (i) participation in self-governing organizations is negatively associated with the "extractive capacity" of grassroots governments (Liu et al. 2012: 191); and that (ii), unlike other forms of non-state provision (e.g., co-production),

“substitutive” public goods provision by community organizations is negatively related to village officials’ ability to complete the tasks assigned by township officials (Tsai 2011: 61). Taken together, these findings can be interpreted as evidence that non-state provision by self-governing organizations negatively affects two key dimensions of (local) state capacity – the capacity to tax (Liu et al. 2012) and to elicit compliance with state policies (Tsai 2011) -, through its negative effects on (local) state legitimacy.

Chapter Two

China's Intergovernmental Fiscal Reforms and Rural Public Finance

2.1 Introduction

There is growing concern that “the unsatisfactory state of the intergovernmental finance system is becoming an increasingly important obstacle to development” in China (Wong and Bird 2008: 454). Since the mid-1990s, the central government has implemented a series of fiscal reforms that have reduced the tax base of local governments, making them increasingly dependent on central transfers to finance their expenditures. There is evidence that the recentralization of the fiscal system has created new challenges to improve government accountability and service delivery, especially in rural areas (e.g., World Bank 2007; Fock and Wong 2008; Wong and Bird 2008). And yet the literature on Chinese federalism (e.g., Montinola et al. 1995; Zhuravskaya 2000; Jin et al. 2005; Weingast 2009) – arguably the most influential strand of literature examining the impact of fiscal institutions on governance and development in reform-era China – does not provide insights into the nature and impact of these reforms.

Against this background, this chapter pursues four main objectives. First, it provides an overview of the evolution of central-local fiscal relations during the reform period. It contrasts the processes of decentralization and recentralization that have shaped central-local fiscal relations under the fiscal contracting system (1980-1993) and the tax-sharing system (1994-present), while highlighting the growth of vertical fiscal imbalances, and the resulting dependence of local governments on transfers, as one of the most important changes in local public finance in recent years. An analysis of the vertical structure of government under the fiscal contracting system and the tax-sharing system shows that, from an expenditure perspective, little has changed: China remains one of the most decentralized countries in the world, with local governments accounting for more than 70 percent of total government expenditures (i.e., expenditure decentralization). However, from a revenue perspective, much has changed with the introduction of the tax-sharing system: China’s reliance on central-local transfers to finance decentralization is today considerably greater than in the past and greater than that of other countries, both developed and developing. Transfers absorb around 60 percent of central revenues

and finance 40-50 percent of local expenditures²⁸ (i.e., revenue centralization) (Wong 2010, 2011; Bahl 2011; Whiting 2011).

In addition to identifying changing trends in local public finance, the chapter also identifies persistent weaknesses in the intergovernmental fiscal system, including: the lack of clear expenditure and revenue assignments at the subnational level, which has resulted in higher levels of local government “pushing down” expenditures and “grabbing” revenues (Wong 2009); the lack of transparency of the intergovernmental transfer system and its limited effectiveness in both closing vertical fiscal gaps and reducing horizontal fiscal disparities (World Bank 2002; Dollar and Hofman 2008; Whiting 2011); and the lack of formal revenue autonomy of local governments, which contrasts with their extensive reliance on various forms of informal taxation and indirect borrowing (Martinez-Vazquez et al. 2006ab; Fock and Wong 2008; Man 2011). These and other problems indicate that, despite successive rounds of reform, China’s intergovernmental fiscal system still remains “a work in progress” (Wong and Bird 2008).

A second objective of this chapter is to assess the impact of fiscal institutions – the intergovernmental fiscal system and interjurisdictional competition – on rural service provision, through their effects on the fiscal resources and incentives of rural governments. During the reform period, counties, townships and villages have assumed the main responsibility for providing basic infrastructure, health, education and social welfare to rural residents (World Bank 2002; Tsai 2007b; Wong and Bird 2008; Fock and Wong 2008; Saich 2008). However, existing studies (e.g., Saich 2008) show that, both under the fiscal contracting system and the tax-sharing system, grassroots governments have lacked adequate resources to meet demands for public services. The emergence of large horizontal and vertical fiscal imbalances has made it difficult for them to finance their provision. Under the fiscal contracting system (1980-1993), the critical factors affecting the availability of resources for service delivery in rural communities were: (i) the uneven distribution of tax bases across rural areas, resulting from the uneven development of township and village enterprises, concentrated in coastal provinces and peri-urban areas; and (ii) the limited ability of the central government to use the transfer system for redistributive

²⁸ Tax rebates are not included.

purposes, due to the decline in government revenues (West and Wong 1995; Wong 1997, 2009, 2010). Under the tax-sharing system (1994-present), two additional factors affecting the availability of resources for rural service provision are: (i) the large mismatch between expenditure and revenue assignments at the county, township and village levels; and (ii) the limited effectiveness of the intergovernmental transfer system in channelling resources to rural governments (World Bank 2002; Martinez-Vazquez 2006; Oi and Zhao 2007; Chen 2008; Dollar and Hofman 2008; Fock and Wong 2008; Martinez-Vazquez et al. 2008ab; Tian 2009; Wong 2009, 2010). According to Wong (2009: 942-943), after four decades of reforms, the intergovernmental fiscal system remains “broken” in the sense that it “lacks mechanisms for ensuring that they [local governments] have adequate financial resources”. However, unlike in the early reform years, the main cause is not the lack of resources at the central level, but rather the lack of a transfer system that effectively redistributes fiscal resources among regions and levels of government.

The availability of fiscal resources is a necessary but not sufficient condition for local governments to meet local demands for services – incentives also matter. Existing studies suggest that interjurisdictional competition has not provided villagers with an effective mechanism to hold local governments accountable for their provision of services. This is for three reasons. First, the *hukou* system has restricted rural-urban migration (e.g., Tsui and Wang 2004). Second, to the extent that local governments have competed with one another for (mobile) production factors, they have competed for capital, not (unskilled) labour (e.g. Montinola et al. 1995). And third, the recent abolition of agricultural taxes has further weakened the “exit” option as a mechanism to hold grassroots officials accountable for the provision of public goods, especially in agricultural villages (Takeuchi 2014).

A consensus emerging from the research and policy literatures is that improving public services in rural China will, at a minimum, require a fundamental and comprehensive reform of the intergovernmental fiscal system which, among other things, increases own revenues for local governments (e.g., Martinez-Vazquez et al. 2006ab; OECD 2006; Dollar and Hofman 2008; Fock and Wong 2008; Shah and Shen 2008). However, in its attempt to improve the financing and delivery of rural services, the central government has taken a very different approach: it has eliminated

rural fees (2002-2004) (e.g., Yep 2004), abolished the agricultural tax (2004-2006) (e.g., Kennedy 2007a) and increased transfers to rural governments under the “New Socialist Countryside” policy (2006-present) (e.g., World Bank 2007). A third objective of this chapter is to analyze China’s recent rural tax reforms and to discuss their potential implications for local governance and public goods provision. Although more research is needed, the available empirical evidence raises questions about the effectiveness of these reforms. Case study evidence of the widespread use of *guanxi* or connections to obtain transfers from higher levels (Liu M. et al. 2009; Schubert and Ahlers 2011; Takeuchi 2014), the growing reliance on illegal land sales as a source of revenues (Takeuchi 2014), the rising levels of local government debt (Bird et al. 2011; Ong 2012), the systematic diversion of (central and local) funds intended for service delivery (World Bank 2007; Liu M. et al. 2009), the increasing over-staffing of local government agencies and the persistent under-provision of local public goods and services (Fock and Wong 2008) provides a glimpse of the challenges that lie ahead for “building a new socialist countryside” under the current fiscal system.

The last objective of this chapter is twofold, and relates to the theoretical implications of China’s move towards a centralized fiscal system. The chapter first seeks to question the way in which “market-preserving federalism” theory is being applied to the comparative analysis of China’s fiscal federal system. The shift from the fiscal contracting system to the tax-sharing system has brought about a fundamental change in the conditions underlying the so-called “federalism, Chinese style” (Montinola et al. 1995; Zhuravskaya 2000; Jin et al. 2005; Weingast 2009) and in the main mechanisms by which fiscal institutions are believed to create incentives for the efficient provision of local public goods, namely, a high degree of *both* expenditure and revenue decentralization and the resulting fiscal competition among local governments for mobile production factors. Recent works on Chinese federalism still characterize China as a “market-preserving federal” system (e.g., Weingast 2009: 282) and view the introduction of the tax-sharing system as a “shift toward a formal fiscal federalism” (Montinola et al. (1995: 72), rather than as a departure from it. These works, however, fail to account for the central government’s centralization of the fiscal system, the growing mismatch between expenditure and

revenue assignments (i.e. vertical imbalance), the increasing dependence of local governments on central transfers, and the implications that all this may have for the incentive structure facing local officials and for their tax effort and spending behaviour. To the extent that China's decentralized system conformed to the ideal of a "market-preserving federal" system under the fiscal contracting system – something that has been called into question (e.g., Cai and Treisman 2004; Tsai 2004; Ong 2012) –, there are grounds to argue that this is no longer the case given that, under the tax-sharing system, China fails to satisfy most, if not virtually all, of the market-preserving federalism conditions. The chapter argues that, while the "market-preserving federalism" literature still provides a useful theoretical framework for examining how fiscal institutions affect the incentives and policy choices of local governments in China, it might be best used to examine the consequences of China's divergence from, rather than convergence with, "market-preserving" federal systems.

A second theoretical implication of China's shift to a centralized fiscal system, the chapter argues, is the need to go beyond the "market-preserving federalism" framework, in order to gain a better understanding of the ways in which the growing mismatch between expenditure and revenue decentralization observed in the country might negatively affect local governance and rural development – ways other than by reducing the fiscal incentives of local governments to expand their tax bases. Against this background, this chapter draws attention to a growing strand of the second-generation fiscal federalism literature – "partial decentralization" theory – (e.g., Khemani 2005; Ahmad and Brosio 2009; Devarajan et al. 2009), which provides a new perspective on the interaction between taxation and governance in decentralized systems, complementing that provided by the market-preserving federalism literature²⁹. Empirical evidence shows that the degree and form of (fiscal) decentralization does not only affect state-business relations or the extent to which local governments "foster and preserve" markets (Weingast 2009), but also affects state-society relations and, more specifically, the extent to which local governments are democratically accountable to their citizens and, consequently, the extent to which citizens trust their local government (e.g., De Mello 2004). The issues of

²⁹ For an overview of the relationship between taxation and governance at the national level, see Bräutigam (2008).

political accountability and legitimacy have, in turn, important implications for the incentives and ability of local governments to provide public goods and to collect taxes, respectively (e.g., Smoke 2011). By examining how recent fiscal reforms have changed the way in which Chinese local governments are financed and by drawing on the recent literature on “partial decentralization”, this chapter raises questions about the impact of these reforms on two critical dimensions of state-society relations that crucially affect (and are affected by) public goods provision: political accountability and legitimacy – questions that will be examined in chapters 3 and 4.

The chapter is structured as follows. Section 2.2 examines the evolution of intergovernmental fiscal institutions under the fiscal contracting system and the tax-sharing system and critically assesses whether they have provided rural governments with adequate fiscal resources to meet local demands for public services. Section 2.3 engages with debates about whether China’s political economy can be described as a “market-preserving” federal system (Weingast 2009: 282) and discusses whether interjurisdictional competition has created fiscal incentives for local governments to meet villagers’ demands for services. Section 2.4 analyzes the rationale, nature and effects of the recent reform of the rural taxation system, in particular, the tax-for-fee reform and the abolition of agricultural taxes. Section 2.5 provides a brief overview of the literature on “partial decentralization” and raises questions that will be explored in subsequent chapters. Finally, section 2.6 provides a summary and concludes.

2.2 The Re-Centralization of Intergovernmental Fiscal Relations

The key to China's public finance system lies in its intergovernmental finance system (Wong and Bird 2008: 429). The analysis of China's intergovernmental fiscal relations under the fiscal contracting system (1980-1993) and the tax-sharing system (1994-present) reveals opposite trends of decentralization and recentralization (e.g., Ahmad et al. 2002; Dabla-Norris 2005). Table 2.1 shows the evolution of the main elements of the intergovernmental fiscal system during the reform period – expenditure and revenue assignments and intergovernmental transfers -. Sections 2.2.1 and 2.2.2 examine the main changes and weaknesses in the system and their implications for rural service provision.

Table 2.1: China's Intergovernmental Fiscal System

	Fiscal Contracting System	Tax-Sharing System
Main objective	○ Increase the tax effort of local governments and put them on a self-financing basis.	○ Strengthen the fiscal capacity of the state and recentralize tax revenues.
Expenditure assignments between central and local governments	○ The pre-reform division of expenditure responsibilities between the central and local governments remained unchanged. The lack of clarity in expenditure assignments facilitated the imposition of unfunded mandates.	○ The Budget Law (1994) has delineated the division of expenditure responsibilities between the central and local governments in broad terms. The lack of a formal assignment of expenditure responsibilities remains a problem. Expenditures have remained decentralized.
Revenue assignments between central and local governments	○ Under the fiscal contracting system, revenues were divided into “central fixed revenues”, “local fixed revenues” and “shared revenues”. Local fixed revenues and shared revenues were divided between the central and provincial governments according to revenue-sharing contracts, which varied across provinces and throughout time. Revenues were decentralized.	○ Under the tax-sharing system, taxes are assigned to the central government (“central taxes”), local governments (“local taxes”) or shared between the central and local governments (“shared taxes”) and revenues from shared taxes are divided between central and local governments according to established formulas. Revenues have been re-centralized.

Table 2.1 (continued): China's Intergovernmental Fiscal System

Central-provincial transfers	<ul style="list-style-type: none"> ○ There were four main types of central-provincial subsidies. (1) “Fixed subsidies” or “quota subsidies” were designed to help poor provinces to finance local expenditures and were governed by revenue-sharing contracts. The three other components of central-provincial transfers were used to implement central policies and to compensate provincial governments for central policy changes and they were not governed by fiscal contracts; (2) “earmarked grants” provided by the central government for specific purposes; (3) “compensatory payments” to local governments for the transfer of local enterprises to central ownership; (4) “final account subsidies” made by the central government to cover provincial budget deficits. 	<ul style="list-style-type: none"> ○ There are three main types of transfers: (1) tax-rebates; (2) general-purpose transfers; and (3) specific-purpose transfers. Tax-rebates provide provincial governments with 30% of the increase in the VAT, consumption tax and income tax collection in the province. General purpose-transfers include “equalization transfers” which are rules-based transfer designed to reduce horizontal fiscal disparities, as well as “pre-tax sharing system grants” which refer to the “fixed subsidies” received by poor provinces under the fiscal contracting system and which are also a component of the new system. Specific-purpose transfers can be divided into: (a) fiscal capacity transfers, such as “transfers for ethnic minority areas”, “transfers for wage adjustments”, “transfers for the tax-for-fee reform”, which are targeted to less developed regions or aimed at supporting or compensating local governments for an increase in expenditure or loss of revenue as a result of policy reforms; and (b) earmarked transfers, which are allocated for specific purposes on an ad hoc basis.
Subnational borrowing	<ul style="list-style-type: none"> ○ No formal authority to borrow. 	<ul style="list-style-type: none"> ○ No formal authority to borrow.
Fiscal authority	<ul style="list-style-type: none"> ○ No formal authority to determine taxes, tax bases or tax rates. 	<ul style="list-style-type: none"> ○ No formal authority to determine taxes, tax bases or tax rates.
Tax administration	<ul style="list-style-type: none"> ○ Local finance bureaux were responsible for collecting most taxes. 	<ul style="list-style-type: none"> ○ Central tax agencies collect “central” and “shared” taxes. Local tax agencies only collect “local” taxes.
Main trends	<ul style="list-style-type: none"> ○ Budgetary decline; decentralization of revenues and expenditures; local fiscal self-reliance; large horizontal imbalances. 	<ul style="list-style-type: none"> ○ End of budgetary decline; recentralization of revenues; high transfer dependence; large vertical and horizontal imbalances.

Sources: Wong (1991, 1997, 2000, 2007ab, 2009, 2010); Montinola et al. (1995); Wong et al. (1995); Zhang (1999); Dabla-Norris (2005); Jin et al. (2005); Shah and Shen (2006); Wong and Bird (2008); Martinez-Vazquez and Qiao (2011); Huang and Chen (2012).

2.2.1 The Fiscal Contracting System

The introduction of the fiscal contracting system in the 1980s led to the decentralization of both expenditure responsibilities and fiscal resources to local governments (Shirk 1993; World Bank 2002; Qian 2003; Tsai 2004; Wong and Bird 2008). Under this system, the central government signed revenue-sharing contracts with each province, which specified the amount of locally collected revenues to be remitted to the central government annually and allowed the provinces to retain the rest. At the same time, provincial governments were required to meet their expenditure responsibilities from their own revenues and were given budgetary autonomy to carry them out. The adoption of the fiscal contracting system represented a departure from the pre-reform system of “unified revenue collection and unified spending”, under which all revenues belonged to, and were budgeted by, the central government (Shirk 1993; World Bank 2002; Qian 2003; Tsai 2004; Wong and Bird 2008). Under the new system, “localities became independent fiscal entities that had both responsibility for local expenditures and the unprecedented right to use the revenue that they retained” (Oi 1992: 103).

An analysis of intergovernmental fiscal relations under the fiscal contracting system (1980-1993) reveals several weaknesses in their design and implementation and explains why it became “unstable, non-transparent and inequitable” (Agarwala 1992: v). First, and most fundamentally, the intergovernmental fiscal reforms of the 1980s were narrow in focus and scope. Greater emphasis was given to providing incentives to local governments for revenue mobilization, than to promoting transparency or equity (e.g., Bahl and Wallich 1992). At the same time, the reform was limited to central-provincial revenue sharing arrangements, while little attention was paid to other dimensions of central-provincial relations, and even less to provincial-local fiscal relations (Bahl and Wallich 1992; Wong et al. 1995; Wong 2007a).

Second, fiscal contracts governing central-provincial revenue sharing were *ad hoc* and subject to continued renegotiation by the central government – often to increase its share of budget revenues. This element of bargaining and uncertainty in central-provincial revenue-sharing arrangements undermined the stability, predictability and transparency of the intergovernmental fiscal system (Wong et al.

1995; Tsai 2004; Tsui and Wang 2004). It also created perverse incentives for provincial officials to reduce the amount of revenues shared with the central authorities and, more specifically, to shift resources “from the budget to off-budget” (Wong 1998: 200)³⁰. The growth of off-budget finance at the local level compounded the problem of “budgetary decline” (Zhang 1999), caused by the falling profitability of state-owned enterprises, and created a problem of “fiscal dualism” (Wong 1998), resulting from the co-existence of a formal and informal system of public finance. By 1993, the size of the budget had declined from 35 percent of GDP to less than 15 percent, while off-budget funds equalled almost 60 percent of the size of the budget (Wong 1998).

Third, the central government failed to establish a clear division of expenditure responsibilities and actually shifted fiscal burdens to provincial governments³¹. The proliferation of unfunded mandates from the central government - ranging from education to birth control – reduced the spending autonomy of the provinces and created strong fiscal pressures for those with weaker fiscal capacities (Wong et al. 1995; Wong 1997; Nyberg and Rozelle 1999; Tsui and Wang 2004; Dabla-Norris 2005; Martinez-Vazquez 2006). Between 1980 and 1993, the central government share of total government expenditures dropped from 54 to 28 percent, reflecting a *de facto* decentralization of expenditure responsibilities to local governments (Zhang 1999; Wong 2000).

Fourth, the ability and willingness of the central government to assist poor provinces and rural areas through fiscal transfers weakened during this period, as it failed to establish an intergovernmental transfer system with the capacity to reduce

³⁰As a result of the “credibility problems” of the central government (Wong et al. 1995), the fiscal contracting system contributed to the very process of budgetary decline it was meant to reverse. The new system actually strengthened the incentives of local governments to increase *off-budget* revenues, which were retained by local governments in their entirety, at the expense of *budget* revenues, which were subject to sharing with the central government according to the terms of their fiscal contract. For instance, a common practice during these years was for local governments to exempt local enterprises from tax payments (i.e. budget revenues) and to impose various fees and levies on their after-tax profits (i.e., off-budget revenues) (Wong 1991, 1998, 2000, 2007a, 2009; Arora and Norregaard 1997; Tsai 2004; Dabla-Norris 2005; Lou 2008; Wong and Bird 2008).

³¹ In practice, local governments at the provincial level and below maintained their pre-reform roles. Like in the pre-reform period, they were responsible for the delivery of basic public services, including education, health and social welfare. The difference with respect to the pre-reform period is that, under the fiscal contracting system, local governments did not only provide these services, but also financed them (Wong et al. 1995; Wong 1997, 2000, 2007ab, 2009).

fiscal disparities across regions and sectors. Under the fiscal contracting system, central-provincial transfers fell from more than 4 percent of GDP in 1986 to 1 percent in 1993, mirroring the decline in (central) government revenues (Wong 2009). Among the three types of central-provincial transfers, only the so-called “fixed subsidies” or “quota subsidies” were aimed at equalization (see Table 2.1), and they represented a declining share of the total, falling from 42 percent in 1980 to 17 percent in 1993³² (Wong et al. 1995; Wong 1997).

Last, the central government did not establish how fiscal decentralization reforms were to be implemented at the subprovincial level, leaving this to the discretion of provincial governments. Fiscal relationships among different levels of local government (i.e., provinces, prefectures/municipalities, counties, townships and villages) ended up replicating those between the centre and the provinces. Also at the subprovincial level, the vertical distribution of revenues was negotiated between adjacent levels of government and formalized in fiscal contracts; expenditure responsibilities were *de facto* devolved to lower levels; and transfers played an equally limited role in redistributing resources from richer to poorer jurisdictions (e.g., Wong 1997).

One of the main implications of the introduction of the fiscal contracting system for local public finance was that local governments were forced to become “fiscally self-reliant” and to generate sufficient revenues to meet their expenditure needs (Park et al. 1996). As pointed out by Zhang (1999: 121), “reforms up to 1993 transformed a province-collecting, centre-spending fiscal regime into an essentially self-financing regime for both the centre and the provinces”. By 1993, local governments accounted for more than 70 percent of total budgetary revenues and expenditures. This trend towards “local self-reliance” in public finance (Park et al. 1996) represented a fundamental change with respect to the pre-reform era and had important implications for rural service provision (Knight and Song 1993; West and Wong 1995; Wong et al. 1995; Park et al. 1996; Wong 1997; Nyberg and Rozelle 1999).

The main one is that, in many parts of rural China, grassroots governments lacked adequate resources to meet their service delivery responsibilities (e.g., Park et

³² In contrast, earmarked grants – most of which were absorbed by price subsidies for grain, oil and cotton, which were targeted at the better-off, urban population – increased from 51 to 66 percent of total central transfers during the same period (Wong et al. 1995; Wong 1997).

al. 1996). The *de facto* devolution of expenditure responsibilities to local governments and the decline in redistributive transfers forced them to rely on their own revenues to provide basic public services (e.g., Wong 2009). While rural enterprise development was “the single most important determinant of a local community’s spending capacity”³³ (Byrd and Gelb 2001: 371), only a relative minority of rural communities had successful township and village enterprises. The geographically uneven distribution of rural industry – concentrated in coastal provinces and peri-urban areas – resulted in an uneven spatial distribution of fiscal capacities and public services across counties, townships and villages (Knight and Song 1993; West and Wong 1995; Zhang and Kanbur 2005).

To summarize, under the fiscal contracting system (1980-1993), the critical factors affecting the availability of resources for rural service delivery were: (i) the uneven distribution of tax bases across rural areas, resulting from the uneven development of township and village enterprises; and (ii) the limited ability of the central government to use the transfer system for redistributive purposes. Against a background of “budgetary decline” (Zhang 1999) and the resulting “collapse of redistribution” (Wong 2009), horizontal disparities in fiscal capacity among counties, townships and villages emerged as the main challenge for the central government to ensure access to basic infrastructure and services for rural residents, particularly in poor agricultural regions.

³³ The main reason is that the Chinese fiscal system has traditionally relied on industry and commerce to generate tax revenues, and that grassroots governments have also relied on rural enterprises to generate non-tax revenues, such as the profits remitted by collective enterprises or the rental payments and fees collected from private businesses (e.g., Wong 1997; Nyberg and Rozelle 1999).

2.2.2 The Tax-Sharing System Reform

In 1994 the central government carried out important reforms in the fiscal arena, including a reform of tax policy, tax administration and intergovernmental finance (e.g., Dabla-Norris 2005; Wong and Bird 2008). The 1994 fiscal reform represented a turning point in central-local fiscal relations - an opportunity to address the problems created, or left unresolved, by the decentralization reforms of the 1980s. Its main aim was to reverse the declining trend in the so-called “two ratios” – revenue/GDP and central/total revenue (Ahmad et al. 2002; Wang 1997; Dabla-Norris 2005; Wong and Bird 2008). In addition to strengthening and recentralizing the fiscal system, the reform was also intended to enhance its transparency and redistributive role (World Bank 2002).

To achieve these goals, the central government replaced what was “a negotiated system of general revenue sharing” (i.e., the “fiscal contracting system”) with what became “a mix of tax assignments and tax sharing” (i.e., the “tax-sharing system”) (Wong and Bird 2008: 434). It established that, under the new tax-sharing system, taxes would be divided into three categories: taxes assigned to the central and local governments (i.e., “central taxes” and “local taxes”); and taxes shared between them according to established formulas (i.e., “shared taxes”) (see Table 2.2). The central government also reformed the tax administration system. It created a national tax bureau that would be responsible for collecting “central” and “shared” taxes, while local tax bureaus would only be responsible for collecting “local” taxes (Wong and Bird 2008: 436).

By defining the new value-added tax (VAT) - the biggest tax - as a “shared tax” and claiming 75 percent of its proceeds, the central government centralized revenues, securing more than 50 percent of the total for itself. And by creating a national tax administration, it centralized tax collection and eliminated opportunities for local governments to divert resources from the formal to the informal fiscal system (Wong and Bird 2008: 434-436). In essence, the 1994 reform changed the way taxes were collected, and the way revenues were shared between central and local governments, strengthening central control over the fiscal system.

Table 2.2: Revenue Assignments: Central, Local and Shared Taxes

Central	Shared	Local
Tariffs	VAT (75% central-25% local)	Business tax (except financial institutions and railroads)
Consumption taxes	Stamp tax (97% central-3% local)	Contract tax
Income taxes of centrally-owned SOEs	Corporate and individual income taxes (60% central – 40% local)	Urban land use tax
Import-related consumption taxes and value-added taxes	Resource taxes (offshore oil-central; remainder-local)	Urban maintenance and development tax (except financial institutions and railroads)
Taxes on financial institutions and railroads		Fixed asset investment adjustment tax
Profits from centrally-controlled SOEs		Profits from locally controlled SOEs
		Housing property tax
		Agricultural taxes
		Tax on use of arable land
		Tax on land value increase

Source: Whiting (2011: 129).

The reform was successful in achieving its main objective – namely, increasing the fiscal capacity of the (central) government (World Bank 2002; Martinez-Vazquez 2006; Wong and Bird 2008). Between 1993 and 2008, budget revenues increased from about 12 to 20 percent of GDP, while the central government's share increased from 22 to 53 percent of the total (Man 2011: 5). However, the reform objectives of increasing transparency in central-local relations and of reducing fiscal disparities across and within provinces have not been fully achieved (World Bank 2002; Tsai 2004). The main reason is that the reform failed to address some of the weaknesses of the previous intergovernmental fiscal system.

A major weakness of the current system is the lack of clear and appropriate expenditure and revenue assignments among levels of government, particularly at the

subprovincial level. As in the 1980s, the intergovernmental fiscal reform was narrowly focused on the revenue side of central-provincial fiscal relations. Little attention was paid to other elements of and actors in the intergovernmental finance system (e.g., Martinez-Vazquez 2006; Martinez-Vazquez et al 2006a, 2008a; Qiao and Shah 2006; Wong 2007a; Dollar and Hofman 2008; Man 2011; Whiting 2011). Although the 1994 Budget Law clarified the division of functions between the central and local governments (see Table 2.3), it did not specify how “local” expenditure responsibilities were to be divided among local governments. Similarly, although the tax-sharing system reform established a clear distinction between “central”, “local”, and “shared” taxes, it did not provide rules for how to distribute revenues from “local taxes” and “shared taxes” among local governments. Once more, the vertical distribution of responsibilities and revenues at the subnational level was left up to the discretion of the provinces.

Table 2.3: Expenditure Responsibilities of Central and Local Governments

Central Government	Subnational Governments
1. National defense	1. Local government administration
2. Diplomacy and foreign affairs	2. Local public services
3. Military police	3. Locally financed basic infrastructure and technical renovations
4. Key construction projects	4. Support to agriculture
5. Central government administration	5. Urban maintenance and construction
6. Public services at the central level	6. Price subsidies
7. Debt service payments	7. Other expenditures

Source: Fock and Wong (2008: 10-11)

The fact that the tax-sharing system reform reduced “local revenues” without adjusting “local expenditures”, and that it did not provide explicit rules about how local governments should divide “local revenues” and “local expenditures” among themselves had unintended negative effects on the local public finance system³⁴. The

³⁴ Recent fiscal reforms have not addressed these problems. On the revenue side, the reform of the tax-sharing system in 2002-03 contributed to make matters worse for local governments, as it further reduced local revenues. With this reform, the central government increased its revenues: it shifted taxes from the “local” to the “shared” category and increased the central share of “shared taxes”

interplay of these factors – the fiscal pressure on local governments to deliver more with less, and the power of higher levels within the local administrative hierarchy to shape their fiscal relations with lower levels - gave way to (informal) processes of revenue (re-)centralization and expenditure decentralization at the subnational level. All local governments – from the provincial to the township level – sought to balance their budgets at the expense of lower-level governments (World Bank 2002; Dabla-Norris 2005; Wong 2007a; Chen 2008; Wong and Bird 2008; Saich 2008; Tian 2009). This is well explained by Chen (2008: 334), who describes how the tax-sharing system reform transformed the distribution of resources and responsibilities at the local level into “a thinly disguised political battle between different administrative layers”. And, in this battle, “each layer of local government vied to replicate the self-serving policy of the center, leading to an upward flow of tax revenues and a top-down imposition of expenditure burdens”.

As a result of these trends, a high vertical fiscal imbalance emerged at the lowest levels of the administrative hierarchy (i.e. counties, townships and villages) (e.g., World Bank 2002). According to Wong and Bird (2008: 12), “the most critical fiscal issues in China today essentially arise from the mismatch of expenditures and revenues between levels of government resulting from the 1994 reform and the resulting distortions as China’s various layers of government struggled to find their fiscal feet in this fundamentally distorted structure”.

A second major weakness of the current intergovernmental fiscal system is related to the limited ability of intergovernmental transfers to address vertical and horizontal fiscal imbalances (e.g., Martinez-Vazquez 2006; Wong 2007ab, 2009, 2010). Tables 2.4 and 2.5 provide a complete list and description of the main components of the transfer system, including tax rebates, general-purpose transfers, and specific-purpose transfers. Figure 2.1 shows the interaction between the main actors in the intergovernmental fiscal arena, and how central government transfers to rural areas must pass through intermediate-level governments (i.e., provinces and

(Martinez-Vazquez et al. 2006a; Qiao and Shah 2006; Wong and Bird 2008; Whiting 2011). On the expenditure side, although the “Suggestions on Sub-provincial Fiscal Relations” issued by the Ministry of Finance in 2002 have provided some general guidelines for the assignment of expenditures to sub-provincial governments, they are mere “suggestions” and, as such, have not constrained the discretionary power of provincial governments in this respect (Qiao and Shah 2006; Martinez-Vazquez et al. 2008a; Martinez-Vazquez and Qiao 2011).

prefectures/municipalities), before reaching rural governments (i.e., counties, townships and villages).

Table 2.4: Classification of Intergovernmental Transfers

I. Tax rebates
1. Tax rebates for consumption taxes and VAT
2. Tax rebates for (corporate and individual) income taxes
II. General-purpose transfers
1. Equalization transfers
2. Pre-tax sharing system grants
III. Specific-purpose transfers
1. Earmarked transfers
a) Education
b) Science and Technology
c) Social Security and Employment
d) Healthcare
e) Environment protection
f) Agriculture, forestry and water conservation
2. Fiscal capacity transfers
a) Transfers for minority regions
b) Transfers for increasing wages of civil servants
c) Transfers for rural tax reform
d) Transfers for rural compulsory education
e) Transfers of resource exhaustion to the cities
f) Other transfers

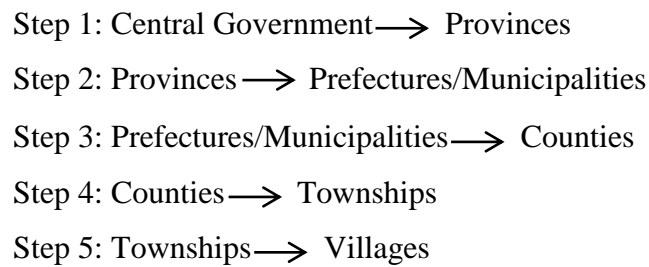
Source: Huang and Chen (2012: 550)

Table 2.5: Central-Provincial Transfers: Vertical and Horizontal Shares

Transfer type	Vertical share	Horizontal share
VAT and excise tax rebate (1994)	The base for the rebate for each province was fixed in 1994, to allow maintenance of its previous level of expenditure. Thereafter, the rebate grows by 30 % of the growth of revenues from these taxes collected in the provinces.	Derivation basis
Income tax rebate (2002)	The amount was fixed in 2002 for each province, to allow it to maintain the previous level of expenditures.	Derivation basis
General transfer (formerly, transitional transfer) (1995)	No fixed share until 2002. Since 2002 the vertical share has included the incremental revenues accruing to the central government from income taxes over the 2001 level.	Needs-based formula
Original system (quota) subsidy (1980s)	No fixed share	Distributed only to poor and ethnic minority provinces. Amounts were fixed in nominal terms in 1987.
Wage increase subsidy (1999)	No fixed share	Subsidy given to the poorer inland provinces, to offset the costs of civil service wage increases.
Minority region subsidy (2000)	No fixed share until 2002. Since 2002, the vertical share has included 80% of the incremental VAT collected in the provinces.	For the 14 provinces and regions with large concentrations of ethnic minority populations. Funding comes from (1) central budget appropriation, and (2) 80% of the incremental VAT collected in the provinces. Half of the second component is returned to the collecting provinces and regions by derivation. The other half is pooled with central appropriations and distributed according to a needs-based formula.
Rural fee reform subsidy (2001), subsidies for agricultural tax reduction and adjusting responsibilities (2003)	No fixed share	All provinces are divided into 4 groups to receive compensation for revenue losses under the rural tax-for-fee reform and the abolition of agricultural taxes, at rates of 100% (central and western grain-producing provinces), 80% (non-grain-producing provinces in central and western provinces), 50% (major grain-producing provinces in the coastal region), and 0% (the rest of provinces).
*Earmarked transfers (1994)	No fixed share	They are allocated on an <i>ad hoc</i> basis and are earmarked for specific purposes.

Sources: Bahl (2011: 261); *Huang and Chen (2012: 539).

Figure 2.1: Transmission of Central Transfers to Rural Areas



Source: Adapted from Fock and Wong (2008: 8).

The poor performance of China's transfer system is result of its poor design and implementation. One of its shortcomings is the lack of predictability and stability of central transfers. Using the taxonomy of transfers developed by Bahl and Linn (1994), Tables 2.5 and 2.6 classify central-local transfers along two dimensions: the method of determining their size (i.e., vertical dimension) and distribution among local governments (i.e., horizontal dimension). With respect to the first of these dimensions, most central transfers – around 75 percent of the total - are discretionary (i.e., no fixed share), in the sense that the total amount of funds to be transferred to local governments is not determined as a fixed share of central government revenues. The main exceptions are “tax rebates”, “general transfers” and “minority region subsidies”, which account for less than one-fourth of the total (Wong 2011). As regards the second dimension, about 50 percent of central transfers, including “earmarked transfers” and “original system subsidies”, are allocated among local governments on an *ad hoc* basis (Huang and Chen 2012). The fact that the vertical and horizontal dimensions of the intergovernmental transfer system – the size of the total grant pool and its distribution among local governments – are largely determined in a discretionary or *ad hoc* way creates uncertainty for local governments and compromises their ability to budget effectively.

Table 2.6: China's Central-Provincial Transfer System

Method of Allocating the Divisible Pool Among Eligible Units	Method of Determining the Total Divisible Pool		
	Specified Share of National or State Government Tax	Ad Hoc Decision	Reimbursement of Approved Expenditures
Derivation	Tax rebates		
Formula	Minority region subsidy; General transfer		Wage increase subsidy
Total or partial reimbursement of costs		Rural fee reform subsidy	
Ad hoc		Original system (quota) subsidy	Earmarked transfers

Source: Adapted from Bahl (2011: 260)

Another shortcoming of the intergovernmental transfer system is its weak equalization potential. An analysis of the evolution of its main components – tax rebates, general purpose transfers and specific purpose transfers - reveals the regressive character of the system and the predominance of disequalizing transfers since it was introduced. As shown in Table 2.7, during the 1990s central transfers were dominated by tax rebates, which in 1999 represented about 53 percent of the total. Their regressivity lies in that they transfer 30 percent of the annual growth in VAT, consumption and income tax revenues to provincial governments on a derivation basis (e.g., Shah and Shen 2006; Wong and Bird 2008). Since the early 2000s, specific-purpose transfers, in general, and earmarked grants, in particular, have become the largest component of the transfer system. They represented about 43 percent of central transfers and 63 percent of specific-purpose transfers in 2009 (Huang and Chen 2012). They are disequalizing in that they often require matching funds from local governments (Yep 2004; Dabla-Norris 2005; Shih and Qi 2007; Liu M. et al. 2009; Huang and Chen 2012). The table also shows that, if equalization transfers – the “general transfer” and the “original system subsidy” – have not reversed the trend of growing regional fiscal disparities in China, is because they have been underfunded (Ahmal et al. 2002; Martinez-Vazquez 2006; Chen 2008;

Dollar and Hofman 2008; Shah and Shen 2008; Whiting 2011). As can be seen in the table below, before 2003 they only accounted for 4-6 percent of central transfers and in 2009 they amounted to approximately 14 percent of the total.

Table 2.7: Types of Central-Provincial Transfers, 1995-2009 (%)

	1995	1997	1999	2001	2003	2005	2007	2009
Tax Rebates	73.72	75.31	53.12	37.75	42.50	33.79	23.79	15.47
General purpose transfers	5.36	6.08	4.73	4.25	6.30	11.24	15.22	14.48
Specific purpose transfers	20.92	18.61	42.15	58.00	51.20	54.98	61.00	70.05

Note: General purpose transfers include the “general transfer” and “original system subsidy”. Specific purpose transfers are divided into “earmarked transfers” and “fiscal capacity transfers”. The latter category includes the “wage increase subsidy”, “rural fee reform subsidy” and “minority region subsidy”.

Source: Calculated from Huang and Chen (2012).

Another problem in the design of the intergovernmental transfer system is that it undermines the autonomy of local governments and the transparency of their finances (e.g., World Bank 2002). This is largely due to the design of “earmarked transfers”, which have become one of the main components of the transfer system. The reason why they constrain the allocative authority of local governments lies in their input-based conditionality and matching provisions (Shah 2006): local governments have no autonomy to decide how to spend the transferred funds (input-conditionality) and they have less flexibility in the use of their own revenues (matching requirements). The reason why they have made the intergovernmental transfer system less transparent is because they are allocated to local governments on an *ad-hoc*, negotiated basis (Ahmad et al. 2004; Dabla-Norris 2005; Qiao and Shah 2006; Fock and Wong 2008).

Another shortcoming of the intergovernmental transfer system has to do with its failure to promote fiscal efficiency and tax effort at the local levels. Some types of transfers create incentives for local governments to engage in bureaucratic expansion and rent-seeking. First, the use of “fiscal capacity transfers” to finance civil service wages has aggravated the problem of overstaffing of local government agencies (e.g., Shih and Qi 2007; Fock and Wong 2008; Guo 2008), especially in

poor regions, where adding staff is seen as “the only mechanism for getting more transfers from higher levels” (Martinez-Vazquez 2006: 127). Second, the non-transparent allocation of earmarked transfers encourages rural governments to lobby central government agencies to obtain funds (Liu and Tao 2007; Liu M. et al. 2009; Huang and Chen 2012). According to Liu M. et al. (2009: 988), “running for programmes (*pao xiangmu*) has become a common method of competing for earmarked funds” among county governments, whose liaison offices in Beijing spend more than 20 billion yuan annually to build and maintain connections with central government officials.

Last but not least, the ineffective functioning of the intergovernmental transfer system makes it vulnerable to “leakages” and “policy distortions” (Wong 2010: 24). The fact that the transfer system is structured in a “hierarchical” way implies that the central government depends on intermediate-level governments both to channel funds to grassroots governments and to monitor their use (Martinez-Vazquez 2006; World Bank 2007; Fock and Wong 2008). However, the central government seems to lack the capacity to ensure, first, that transfers reach rural governments, and, second, that they are used for their intended purpose (World Bank 2002, 2007; Martinez-Vazquez 2006; Fock and Wong 2008; Wong 2009, 2010, 2011).

Given the shortcomings of the tax-sharing system, what implications did the 1994 fiscal reforms have for rural governance? The reform did not put an end to the problem of under-provision of public services in rural areas (e.g., Wong 2007ab). Actually, it triggered a fiscal crisis at the county, township and village levels (e.g., Wong 2007a; Chen 2008, 2015; Fock and Wong 2008). Practices of “coercive taxation” became one of the main sources of social unrest in the rural areas of inland provinces, where “predatory state agents imposed heavy financial burdens on the peasants” (Bernstein and Lü 2000: 742). In coastal provinces, where land sales became an important and lucrative source of revenues for local governments, it was “government coercive land expropriation” (Guo 2001: 422) that generated protests from farmers. The response of the central government to the rapid increase in rural protests and to the resulting deterioration in cadre-villager relations (e.g., Bernstein and Lü 2003; Yep and Fong 2009) was to eliminate rural fees (2002-2004) (e.g., Yep 2004), abolish the agricultural tax (2004-2006) (e.g., Kennedy 2007a), and to

increase transfers to rural governments under the “New Socialist Countryside” policy (2006-present) (e.g., World Bank 2007).

Twenty years after the implementation of the tax-sharing system reform, China has one of the largest vertical fiscal imbalances in the world, which exceeds that of other developing and transitional economies (Fock and Wong 2008; Man 2011; Whiting 2011; Wong 2010, 2011). In 2010, local government revenues amounted to about 49 percent of total government revenues, while local government expenditures represented around 82 percent of the total (China Statistical Yearbook 2011). At the same time, China still lacks a transfer system that effectively redistributes fiscal resources among regions and levels of government: one of the main challenges to improve local service delivery is, in the words of Wong (2009: 951), “how to channel resources effectively to where they are needed (...)”. In the absence of an effective intergovernmental transfer system, the growth of vertical fiscal imbalances at the local level constitutes one of the most important obstacles to improve the level and quality of public services in rural communities.

2.3 Interjurisdictional Competition

In first- and second- generation theories of fiscal federalism interjurisdictional competition is viewed as an important institutional mechanism, first, for allowing individuals and firms to sort themselves into jurisdictions whose revenue and expenditure patterns best suit their preferences (e.g., Tiebout 1956); and, second, for aligning the interests of local governments with those of taxpayers and preventing problems of “state predation” and “soft budget constraints” (e.g., Qian and Weingast 1997) (see Box 2.1).

Box 2.1: Fiscal Federalism Theories

First- and second- generation theories of fiscal federalism stress the potential of decentralization to improve the quality of governance and public goods provision, although partly for different reasons (Lockwood 2006, 2009; Oates 2005). From the perspective of traditional theories of fiscal federalism, the reason why decentralization is often preferable to centralization is that localities differ in their preferences for public goods³⁵ (Tiebout 1956; Oates 1999, 2005). The decentralized provision of local public goods has two main advantages (Tiebout 1956; Oates 1999, 2005). First, local governments have better *information* than the central government about local preferences and needs. Second, under decentralization, households and firms can sort themselves into those jurisdictions whose fiscal packages (i.e., tax rates and public goods) best suit their preferences. Hence, decentralization can improve *allocative efficiency* in the provision of local public goods.

New theories of fiscal federalism suggest that decentralization may be preferable to centralization even when localities do not differ in their public goods preferences (e.g., Seabright 1996; Weingast 2009). Unlike first-generation fiscal federalism, this literature does not assume that the government is benevolent and seeks to maximize social welfare, but rather assumes that “public officials have goals induced by political institutions that often diverge from maximizing citizen welfare” (Weingast 2009: 279). From this perspective, decentralization is seen as a way of providing public officials with *fiscal and political incentives* to serve the interests of citizens. By increasing government accountability, decentralization can improve *productive efficiency* in the provision of local public goods.

Within the second-generation fiscal federalism literature, two main strands can be distinguished. One strand stresses the role of fiscal institutions – the intergovernmental fiscal system and interjurisdictional competition - in aligning the interests of government officials with citizens under decentralization (e.g., Weingast 1995, 2009, 2014; Qian and Weingast 1997; Rodden 2003). From this perspective, the two main channels through which decentralization can increase government accountability are: (i) by giving local governments the right and responsibility to generate a significant portion of their revenues (i.e., local revenue generation); and (ii) by placing local governments in competition with each other to attract mobile production factors (i.e., interjurisdictional competition).

A second strand of this new literature draws attention to political institutions and compares their performance in centralized and decentralized systems. It argues that decentralization can increase the ability of citizens to hold government to account through elections and other forms of participation (e.g., Belleflamme and Hindriks 2005; Barankay and Lockwood 2007; Besley and Case 1995; Khemani 2001; Seabright 1996; Persson and Tabellini 2000; Tommasi and Weinschelbaum 2007).

³⁵ Oates’ Decentralization Theorem states that “in the absence of cost-savings from the centralized provision of a good and of interjurisdictional external effects, the level of welfare will always be as high (and typically higher) if Pareto-efficient levels of consumption are provided in each jurisdiction than if *any* single, uniform level of consumption is maintained across all jurisdictions” (Oates 2011: 54).

This is due to the information and incentives available to political actors in decentralized systems, but not in centralized systems. Under decentralization, voters are likely to be better informed about government performance as a result of: (i) the greater “proximity” between citizens and government (Khemani 2001); (ii) reduced “collective action problems” among voters in monitoring government (Tommasi and Weinschelbaum 2007); and (iii) “yardstick competition” among local governments (Belleflamme and Hindriks 2005; Besley and Case 1995). At the same time, locally elected officials are likely to have stronger incentives to respond to citizens’ needs and demands, given that the link between government performance and election outcomes is stronger under decentralization (Seabright 1996). In sum, from the perspective of second generation fiscal federalism, the main rationale for decentralization is one of redistributing power both within the state and between state and society, so as to create the institutional checks and balances required to improve governance and public goods provision.

The market-preserving federalism literature highlights that, under decentralization, taxpayers can hold local governments accountable for their tax and spending decisions, by threatening to “exit” to another jurisdiction and, ultimately, by “voting with their feet” (Weingast 1995, 2009; Qian and Weingast 1997; Qian and Roland 1998; Qian 2003). It is thus assumed that factors of production (i.e., labour and capital) can freely move across jurisdictions; that local governments compete with one another *both* for capital and labour; and that intergovernmental competition for mobile factors is efficiency- and welfare-enhancing (e.g., Bardhan 2002; Bardhan and Mookherjee 2006b).

To what extent is this the case in developing countries in general and China in particular? Has interjurisdictional competition provided Chinese rural governments with fiscal incentives to respond to citizen demands for public goods and services? There is disagreement about the nature and effects of interjurisdictional competition in China and, in particular, about its role in making local governments more accountable. On one side of the debate, an influential strand of the literature contends that post-reform China is a market-preserving federal system and as such is largely characterized by the existence of³⁶: (i) a hierarchy of governments with a clearly defined scope of authority (the “hierarchy” condition); (ii) local governments with authority over the local economy (the “subnational autonomy” condition); (iii) a common market with free movement of products and factors (the “common market”

³⁶ The list of market-preserving federalism conditions is based on and draws heavily upon Montinola et al. (1995: 55) and Weingast (2009: 281).

condition); (iv) hard budget constraints at the central and local levels (the “hard budget constraints” condition); and (v) institutionalized constraints on the power of the central government to reduce local government autonomy (the “institutionalized authority” condition) (Montinola et al. 1995; Weingast 1995, 2009; Qian and Weingast 1997; Jin et al. 2005).

According to this body of literature, one of the main mechanisms by which market-preserving federal systems promote government accountability and economic growth is by placing local governments in competition with one another for investment and, in the view of scholars such as Gabriella Montinola, Yingyi Qian and Barry Weingast (1995), China is a case in point. They argue that fiscal competition has provided local governments with incentives to adopt “pro-market policies” and to provide “market-enhancing public goods” during the reform period (Weingast 2009). It has created incentives for them to support the development of the private sector and to undertake management and ownership reforms in the state and collective sectors (Montinola et al. 1995; Weingast 1995; Qian and Weingast 1997; Qian and Roland 1998; Cao et al. 1999; Qian 2003; Jin et al. 2005). It has also hardened their budget constraints, while increasing the share of their budgets allocated to infrastructure and other public goods (Qian and Roland 1998). For these reasons, they argue, local governments have been “the great engine of economic growth” in China during the past four decades (Weingast 2009: 282).

On the other side of the debate, a growing number of studies argue that it should not be assumed that reform-era China represents a clear-cut example of “market-preserving federalism”, nor that interjurisdictional competition reduces “corruption, predation, and rent-seeking” (Weingast 2009: 282) at the local level. This is for two reasons. The first one is that China’s governance structure simply cannot be characterized as a market-preserving federal system (Tsai 2004; Tsui and Wang 2004; Ong 2012). An analysis of the evolution of central-local relations during the reform period shows that, under the fiscal contracting system (1980-1993) and the tax-sharing system (1994-present), China’s institutional structure has failed to satisfy an increasing number of the market-preserving federalism conditions, despite claims to the contrary (e.g., Weingast 2009). According to scholars such as Kellee Tsai (2004) and Lynette Ong (2012), amongst others (e.g., Tsui and Wang 2004), under

the fiscal contracting system, the fiscal autonomy of local governments was constrained by the proliferation of central policy mandates (the “subnational autonomy” condition) (Tsui and Wang 2004); the central government was unable or unwilling to remove barriers to the mobility of goods, services and factors of production across jurisdictions (the “common market” condition) (Tsai 2004; Tsui and Wang 2004); local governments had easy access to loans from local credit institutions and faced soft budget constraints (the “hard budget constraints” condition) (Tsai 2004; Ong 2012); and the decentralization process was subject to the discretionary control of the central government, as manifested for instance by the continual renegotiation of revenue-sharing contracts between the centre and the provinces (the “institutionalized authority” condition) (Tsai 2004; Tsui and Wang 2004).

Although the focus of these studies is on central-local relations during the early reform years, their argument – that China cannot be characterized as a market-preserving federal system – seems even more valid today. First, the absence of a constitutional or legal basis for decentralization in China (e.g., Smoke 2005) has allowed the central government to re-centralize the fiscal system, mainly through the tax-sharing system reform (e.g., Oi et al. 2012) (the “institutionalized authority” condition). Second, and relatedly, the growing dependence of local governments on transfers from the central government, most of which are earmarked for specific purposes (e.g., World Bank 2007), has reduced their fiscal autonomy (the “subnational autonomy” condition), while softening their budget constraints (the “hard budget constraint” condition) (e.g., Liu and Tao 2007). And, third, these changes have gone hand in hand with the continued presence of restrictions to labour mobility within the country (the “common market” condition) (e.g., Chan and Buckingham 2008). Hence, after more than four decades of reforms, there are more reasons to question the depiction of China’s decentralized system as a market-preserving federal system, and they are to be found mainly within the fiscal system itself.

A second and related reason why interjurisdictional competition has failed to make local governments more accountable in China is related to the inefficient forms that it has taken and the unintended consequences that it has had. If China is not a

market-preserving federal system, it follows that it cannot generate efficient interjurisdictional competition. Chinese federalism should not be characterized as “market-preserving”, but rather as “market-thwarting” (Tsai 2004), “state-corroding” (Cai and Treisman 2004) or even “predatory” (Shih et al. 2004). Under the fiscal contracting system, local governments responded to competition from other jurisdictions for mobile capital, by closing their economies (e.g, Tsai 2004), and by colluding with local businesses to evade central taxes and regulations (e.g., Cai and Treisman 2004). As a result, interjurisdictional competition “thwarted” market forces (Tsai 2004), while “corroding” the capacity of the central government (Cai and Treisman 2004) to prevent and mitigate the potential negative effects of decentralization – both the anticipated (e.g., inter-territorial inequalities) and unanticipated ones (e.g., local protectionism) (Rodden and Rose-Ackerman 1997).

China’s WTO accession and the centralization of its fiscal system and regulatory bureaucracies (e.g., Mertha 2005) put an end to the problems of local protectionism and weak central state capacity but new problems have arisen. Under the tax-sharing system, a new type of “predatory fiscal federalism” (Shih et al. 2004; Shen et al. 2012) has emerged - one in which higher levels of government maximize their budgets by centralizing revenues and decentralizing expenditures (Chen 2008), leaving grassroots governments with “no choice but either to predate on local residents, enterprises and financial institutions or simply not to provide the primary public services” (Shen et al. 2012: 29). In recent years, interjurisdictional competition has also been increasingly associated with fiscally strapped local governments either “running” to Beijing for transfers (e.g., Liu M. et al. 2009), or “racing to the bottom” in taxes (e.g., Yao and Zhang 2008)³⁷. None of this is what one would expect to see in a market-preserving federal system.

³⁷ Under the tax-sharing system, there has been increased competition among local governments for central transfers, especially in inland regions. Rather than promoting local business development, local governments seem to focus their efforts on lobbying central government officials in order to obtain more (earmarked) transfers (Liu and Tao 2007; Shih and Qi 2007; Liu M. et al. 2009). Unlike in inland regions, in coastal provinces, competition among revenue-starved governments to attract domestic and foreign capital has become intense. The problem is that such competition is taking the form of a “race to the bottom” (Yao and Zhang 2008), as local governments compete by offering preferential tax treatment to investors, mainly through tax refunds, which results in tax revenue losses of between 20 and 30 percent annually (Choi 2009: 167-176). Unlike in the past, this form of “informal tax competition” (Choi 2009) is not reducing the revenues of the central government, but those of local governments.

We can draw two main conclusions from this discussion that are directly relevant to our research. First, these studies suggest that, at best, even when and where interjurisdictional competition has been “market-preserving”, it has only made local governments more responsive to the needs of capital, but not of (rural) labour³⁸. An important reason is the existence of the *hukou* system, which has restricted rural-urban migration. Under this system, rural-urban migrants with an agricultural *hukou* status – that is, the majority of them – have been often required to pay rural taxes and fees, while being denied access to urban public services (e.g., Tsui and Wang 2004). A related and more fundamental reason is that, to the extent that local governments have competed with one another for (mobile) production factors, they have competed for capital, not (unskilled) labour (e.g. Montinola et al. 1995)³⁹. This may explain the finding that “growth-oriented local governments favour the interests of capital at the expense of the interests of the general workforce and local residents” (Wang et al. 2009: 146). A third possible reason is related to the recent abolition of agricultural taxes, which has further weakened the “exit” option as a mechanism to hold grassroots officials accountable for the provision of public goods in agricultural villages (Takeuchi 2014). In sum, interjurisdictional competition in China has not provided local officials with strong fiscal incentives to respond to villagers’ needs and demands.

A second conclusion or implication is that the “market-preserving federalism” framework might be best used for examining the consequences of China’s divergence from, rather than convergence with, market-preserving federal systems. The centralization of the Chinese fiscal system (on the revenue side) has brought about a fundamental change in the conditions underlying the so-called “federalism, Chinese style” (e.g., Montinola et al. 1995) and in the mechanisms by which fiscal institutions are believed to increase government accountability, namely, a high degree of *both*

³⁸ At best, the positive effects of interjurisdictional competition have been limited to enhancing the productive efficiency, but not the allocative efficiency, of public expenditures in rich regions: interjurisdictional competition for capital may lead to lower taxation and lower administrative expenditures in these regions, but also to lower spending on public social services such as healthcare (Zhang 2006; Zhang and Chen 2007).

³⁹ Indeed, even scholars who view China as a market-preserving federal system, acknowledge that local governments in inland provinces are actually competing to “export labour” to coastal provinces and to attract remittances from rural-urban migrants (Montinola et al. 1995: 76).

expenditure and revenue decentralization and the resulting competition among local governments to attract mobile production factors. Today, there are compelling reasons to call into question the description of China's governance system as a "market-preserving federal system" and to ask what implications this has for "local state corporatism" (Oi 1992, 1995, 1999) and the developmental role of local governments.

2.4 Rural Fiscal Reforms

Since the early 2000s, the Chinese central government has increased its efforts to promote rural development with the objective of addressing the main problems related to "agriculture", "farmers" and "rural society" (*sannong wenti*) (Fock and Wong 2008). Between 2002 and 2006, the central authorities enacted the "tax-for-fee" reform and abolished the agricultural tax (Yep 2004; Kennedy 2007a; World Bank 2007; Fock and Wong 2008; Göbel 2010). In 2006, the central government set the goal of building a "New Socialist Countryside" and called for "extending public finance and service delivery into the rural areas" (Fock and Wong 2008: 7). During these years, the main focus of its rural reform policies has gradually shifted from one of reducing tax burdens for farmers to one of increasing fiscal transfers to rural governments and improving rural service provision (World Bank 2007; Fock and Wong 2008; Li L.C. 2008).

Introduced in 2002 and heralded as the "third rural revolution" (Göbel 2010), the tax-for-fee reform consisted of: (i) the elimination of all major fees levied by township and village governments and; (ii) an increase in the agricultural tax rate and the introduction of an agricultural tax supplement (Chen 2008, 2015). This reform was intended not only to eliminate the "peasant burden" problem, but also to "bring township and village finance more fully into the budget" (Fock and Wong 2008: 45).

The central government determined that any revenue losses resulting from the implementation of the reform were to be offset by increased central transfers and by reduced local spending. As part of the reform, it created a new transfer program in 2001 (i.e., "grants for rural tax reform") with the objective of reducing the revenue gap of townships and villages (Fock and Wong 2008: 48), and required grassroots

governments to adopt complementary administrative and participatory reforms to increase the (productive and allocative) efficiency of their spending (see Box 2.2) (Fock and Wong 2008; Li L.C. 2008, 2009; Tian 2009; Göbel 2010).

Box 2.2: The Tax-for-Fee Reform
<p>Main components of the fiscal reform:</p> <ul style="list-style-type: none"> • Abolishing all major township and village fees • Abolishing the slaughter tax • Gradually abolishing labour corvées • Increasing the agricultural tax rate to 7% • Standardizing the special products tax • Introducing an agricultural tax supplement equivalent to up to 20% of the value of the new agricultural tax <p>Other measures:</p> <ul style="list-style-type: none"> • Merging townships and villages to reduce the number of territorial units • Reducing the number of offices and employees in rural governments • Regulating strictly the recruitment, evaluation, remuneration and promotion of local government employees • Outsourcing public services • Separating government and business • Creating a supervisory team for burden reduction • Implementing the “yi shi yi yi” system requiring the democratic approval of village-level public projects directly financed by villagers <p>Source: Adapted from Göbel (2010: 88-89)</p>

Township and village governments were encouraged to merge, downsize and, in some cases, to convert state-run public service units into non-state market entities, in order to reduce their current expenditures (Fock and Wong 2008; Li L.C. 2008; Tian 2009; Göbel 2010). As for their capital expenditures, village governments were required to implement the so-called “one undertaking, one decision” (*yi shi yi yi*) policy and empower villagers to decide, by majority vote, on the number and type of village investment projects to be undertaken in their communities, as well as on the amount of money that each household should contribute (Chen 2008; Fock and Wong 2008; Li 2009; Göbel 2010; Yi et al. 2011).

The tax-for-fee reform achieved its main objective and reduced the “peasant burden” (Bernstein and Lü 2003) which, only one year after its introduction, had fallen by around 45 percent nationwide (Yep 2004; Kennedy 2007a; Oi and Zhao 2007; Chen 2008; Tian 2009; Göbel 2010). However, the reform had a negative impact on township and village finances and on rural service provision (Yep 2004;

Kennedy 2007a; Oi and Zhao 2007; Göbel 2010; Alm and Liu 2013)⁴⁰. One of the reasons was that fiscal transfers from the central and provincial governments were not sufficient to compensate grassroots governments for their loss of revenue (Fock and Wong 2008). The other reason was that the New Public Management-style reforms on which the success of the tax-for-fee reform partly depended – the reduction of government personnel and, to a less extent, the adoption of some form of participatory budgeting in village communities (i.e., “yishi yiyi” system) (e.g., Li 2009) – were not effectively implemented. Neither were rural governments willing to cut on administrative costs; nor were villagers willing to contribute to the funding of public projects (e.g., Oi and Zhao 2007; Chen 2008). As a result, the implementation of the “tax-for-fee” reform further reduced the resources available to township and village governments for infrastructure and service provision.

In late 2003, when there were concerns about the gradual “hollowing out” of grassroots governments and it became imperative to find solutions to the rural fiscal crisis, the central government was faced with a critical decision: whether to decentralize or further re-centralize the fiscal system and, more specifically, whether to grant (formal) revenue-raising power to local governments or, instead, rely more on the use of transfers to fill their fiscal gap (Oi et al. 2012: 654). Taking the second option, the central government called for the elimination of the new agricultural tax and, once more, committed itself to increasing fiscal transfers to county, township and village governments, so as to fully compensate them for their loss of revenue (Li 2006; Fock and Wong 2008; Göbel 2010).

In a sense, the abolition of agricultural taxes brought more of the same: it reduced taxes for farmers but it also aggravated the problem of underprovision of public goods and the crisis of local governance in rural areas (Li L.C. 2008). Once more, central transfers failed to reach rural governments and to fill the revenue gap created by the abolition of these taxes (Oi and Zhao 2007; Chen 2008; Fock and Wong 2008; Göbel 2010).

From another perspective, the elimination of agricultural taxes and the aggravation of the rural fiscal crisis brought about a turning point in rural

⁴⁰ Anhui Province, for instance, recorded a decrease of 1.84 billion yuan in revenue for villages and townships after the first year of its implementation, representing a 30-40 percent drop for each village and township on average (Yep 2004).

development policies. It represented the end of a failed “third rural revolution” (2000-2006) and the first step towards “building a new socialist countryside” (2006-present). The focus of rural fiscal reforms shifted to increasing government spending on rural public services and infrastructure (Kennedy 2007a; Li L.C. 2008; Göbel 2010). Promulgated in 2006, the “New Socialist Countryside” policy represents a new commitment on the part of the central government to “extract less, put more back in, and enliven the rural sector” (World Bank 2007: 1). Between 2003 and 2009, central government funding for “agriculture”, “villages” and “farmers” (e.g., the so-called “three rurals”) increased from 214.4 to 725.3 billion yuan (Lin and Wong 2012: 23). During these years, the central government has increased investment in rural infrastructure; implemented a new rural cooperative medical scheme, a free rural compulsory education program, and a minimum living allowance scheme; as well as introduced subsidies for grain production, amongst others initiatives (see Table 2.8) (World Bank 2007; Fock and Wong 2008; Ahlers and Schubert 2009; Lin and Wong 2012; Schubert and Ahlers 2012b; Unger 2012).

Table 2.8: “Building a New Socialist Country”: Major Programs

Program	Year	Objective	Content
Rural minimum living stipend	2005	Provide income support for the poor.	All households with incomes below local stipulated minimum can apply for top-up.
New rural cooperative medical scheme	2005	Provide insurance for rural families to reduce financial risks caused by illness.	Designed mainly for inpatient services; risk-pooling is at the county level. Minimum funding was initially set at Rmb 30 annually per participant, and ratcheted up to Rmb 100 by 2009. Central government pays 40%; local governments pay 40%; and participants pay 20%.
Free rural compulsory education	2006	Eliminate out-of-pocket costs of basic education and boost rural school spending.	Government provides funding to replace school revenues previously collected from miscellaneous fees, and provides subsidy to boarding students from poor families.

Source: Wong (2010: 21)

Although more research is needed, the available empirical evidence suggests that these reforms have aggravated the problems associated with a high vertical fiscal imbalance and transfer dependency at the grassroots level. On the revenue side, the local fiscal gap has not been closed by central transfers and, although rural governments no longer rely on the imposition of illegal fees and levies on farmers, they rely more heavily on land and assets sales, as well as on debt, to finance their expenditures – practices that are economically, socially and environmentally unsustainable (Fock and Wong 2008; Bird et al. 2011; Whiting 2011; Liu 2012; Takeuchi 2013, 2014). On the expenditure side, there are still problems of overspending and misallocation of resources, the latter being manifested by an increase in patronage spending (e.g., public jobs) at the expense of public goods spending (e.g., infrastructure) (Liu and Tao 2007; Fock and Wong 2008; Liu M. et al. 2009). While these problems are not entirely new, recent econometric evidence suggests that they have been compounded by the increasing importance of central transfers in local public finance (Guo 2008; Duan and Zhan 2011; Jia et al. 2014).

2.5 Making Decentralization Partial?

The expansion of the transfer system under the “New Socialist Countryside” programme constitutes the culmination of a process of fiscal recentralization which began with the introduction and adjustment of the tax-sharing system (1994; 2002-03), and continued with the implementation of the tax-for-fee reform (2002-04) and the abolition of agricultural taxes (2004-2006). These reforms have gradually eroded the revenue base of local governments, especially of those at the bottom of the administrative hierarchy (e.g., Fock and Wong 2008). Since the mid-1990s, the central government has fully or partially recentralized the most lucrative taxes, including the consumption tax (100% central), the value added tax (75% central-25% local), as well as (enterprise and individual) income taxes (50% central-50% local in 2002; 60% central-40% local since 2003). At the same time, it has eliminated various local taxes and fees, most notably the agricultural tax (2004-06) and township and village fees (i.e., *jiti tiliu and tongchou fei*) (2002-04) (Martinez-Vazquez et al.

2006a; Qiao and Shah 2006; World Bank 2007; Chen 2008; Fock and Wong 2008; Wong and Bird 2008; Whiting 2011).

The implementation of these fiscal reforms has created a large vertical imbalance between the central and local governments (see Tables 2.9 and 2.10). As can be seen in Table 2.9, while the local share of total revenues has declined since the mid-1990s, local governments have accounted for a larger share of total government expenditures. The resulting gap must be filled by transfers. Generally speaking, the existence of a vertical imbalance in favour of the central government is not only unavoidable, but also desirable, to the extent that it provides the central government with the necessary fiscal resources to reduce local fiscal disparities, and to finance the provision of public goods with positive externalities that would otherwise be under-provided by local governments (e.g., Dabla-Norris 2005; Bahl 2011). However, the Chinese case does not conform to international best practice. China has a larger vertical imbalance than most other countries (see Table 2.11) and it has become an “outlier” in terms of transfer dependency (Fock and Wong 2008; Bahl 2011). In recent years transfers (excluding tax rebates) have absorbed more than 60 percent of central revenues and financed around 40 percent of local expenditures (Wong 2010, 2011; Whiting 2011) (see Table 2.12). At the same time, the intergovernmental transfer system has failed to ensure revenue adequacy at the local level and equalization across jurisdictions (World Bank 2002; Dollar and Hofman 2008; Whiting 2011).

Table 2.9: Local Share of Revenues and Expenditures (1980-2010)

Year	Government Revenues			Government Expenditures		
	Total (100 mln yuan)	Central Share	Local Share	Total (100 mln yuan)	Central Share	Local Share
1980	1159.93	24.52	75.48	1228.83	54.26	45.74
1985	2004.82	38.39	61.61	2004.25	39.68	60.32
1990	2937.10	33.79	66.21	3083.59	32.57	67.43
1995	6242.20	52.17	47.83	6823.72	29.24	70.76
2000	13395.23	52.20	47.80	15886.50	34.70	65.30
2005	31649.29	52.29	47.71	33930.28	25.86	74.14
2010	83101.51	51.10	48.90	89874.16	17.80	82.20

Source: China Statistical Yearbook, various years.

Table 2.10: Vertical Imbalance of Rural Governments

(percent)	1992	1994 Tax-sharing system reform	1998	2000	2002	2004
County and township share of total expenditures	30.9		28.2	26.2	28.6	31.3
County and township share of total revenues	30.1		20.3	19.7	17.1	17.2
Vertical imbalance for counties and townships	-0.8		-7.9	-6.5	-11.5	-14.1

Source: Adapted from World Bank (2007: 23).

Table 2.11: Local Share of Revenues and Expenditures in various Countries

Item	Developing Countries	OECD Countries	Transition Economies	China
Local share of government tax revenue	9	19	17	40
Local share of government expenditure	14	32	26	73

Source: Dollar and Hofman (2008: 40)

Table 2.12: Central Transfers to Local Governments (2012)

Item	Tax Rebates and Transfers		Transfers (excluding tax rebates) as percent of central government revenues	Transfers (excluding tax rebates) as percent of local government expenditures
	Trillion Yuan	Shares		
Tax Rebates	0.512077	11.3%	-	-
General Transfer Payments	2.147118	47.3%	36.5%	19.7%
Special Transfer Payments	1.879152	41.4%	31.9%	17.2%
Total	4.538347	100%	68.4%	36.9%

Source: Budget Report, 2012. Available from: http://english.gov.cn/official/2012-03/16/content_2093602.htm [Accessed 24 June 2014].

This implies that the recentralization of tax revenues and the increase in central transfers to local governments has not resulted in a reduction of horizontal fiscal disparities (e.g., Dollar and Hofman 2008), while the growth of vertical fiscal imbalances may have created new challenges for the accountability of local governments.

What challenges? A recent strand of the second-generation fiscal federalism literature argues that the accountability benefits of decentralization are often not achieved because decentralization is “partial” (Khemani 2005, 2007a; Ahmad et al. 2006; Ahmad and Brosio 2009; Bardhan 2009; Devarajan et al. 2009; Lockwood 2009; Weingast 2009, 2014). “Partial decentralization” is described as “a state of the (decentralized) world where political and fiscal institutions are not able to ensure accountability of local elected politicians and officials” (Ahmad and Brosio 2009: 5). While this may be due to various factors, it typically occurs when “local governments lack control over tax instruments at the margin, so that they remain dependent on central government grants and revenue shares and correspondingly are less accountable to their electorates” (Ahmad and Brosio 2009: 5). Empirical evidence from Asia, Africa and Latin America suggests that what generally makes decentralization “partial” is that political decentralization is not accompanied by fiscal decentralization: democratically elected local governments are created but they are denied control over fiscal resources - whether *de jure* or *de facto* (see Table 2.13) (e.g., Díaz-Cayeros et al. 2003; Olowu 2003; Smoke 2003; Khemani 2005; Devarajan et al. 2009; Weingast 2009, 2014). At the same time, the lack of fiscal decentralization undermines the meaningfulness and effectiveness of political decentralization: citizens are provided with new arenas for political participation, but with little reason or motivation to engage in local politics in order to improve how public funds are spent and what services are provided in their communities. Essentially, the reluctance of the central government to devolve *fiscal authority* to (elected) local governments ends up reducing their *political accountability* to citizens and, as a result, worsens problems of corruption and misallocation of resources at the local level.

Table 2.13: Forms of Decentralization and Public Service Delivery

<i>Degree of decentralization</i>	<i>Political Features</i>	<i>Fiscal Features</i>	<i>Administrative Features</i>
<i>Deconcentration</i> (minimal change)	<ul style="list-style-type: none"> • No elected local government. • Local leadership vested in local officials appointed by and accountable to the central government. 	<ul style="list-style-type: none"> • Local government is a service delivery arm of the central government and has little or no discretion over how or where services are provided. • Funds come from the center. • No independent revenue sources. 	<ul style="list-style-type: none"> • Provider staff working at local level of center, and accountable to the center, usually through their ministries; weak local capacity is compensated for by central employees.
<i>Delegation</i> (intermediate change)	<ul style="list-style-type: none"> • Local government may be led by locally elected politicians, but it is still accountable, fully or partially, to the center. 	<ul style="list-style-type: none"> • Spending priorities are set centrally, as well as program norms and standards; local government has some management authority over allocation of resources to meet local circumstances. • Funding is provided by the center through transfers. • No independent revenue sources. 	<ul style="list-style-type: none"> • Providers could be employees of central or local government, but pay and employment conditions are typically set by the center. • Local government has some authority over hiring and location of staff, but less likely to have authority over firing.
<i>Devolution</i> (substantial change)	<ul style="list-style-type: none"> • Local government is led by locally elected politicians expected to be accountable to the local electorate. 	<ul style="list-style-type: none"> • Subject to meeting nationally set minimum standards, local government can set spending priorities and determine how best to meet service obligations. • Funding can come from local revenues and revenue-sharing arrangements and transfers from the center. 	<ul style="list-style-type: none"> • Providers are employees of local government. • Local government has full discretion over salary levels, staffing numbers and allocation, and authority to fire and hire.

Source: Evans and Manning (2004: 22)

The empirical literature describes two main instances of “partial decentralization”, in which the fiscal dependence of local governments on the central government undermines the role of local elections in making them more accountable to their constituents, although for different reasons and through different channels. The first and main reason has to do with how a centralized and poorly designed fiscal system may weaken the accountability relationship between voters and local officials, through its (negative) effects on *political participation*. There are three main channels through which the “fiscal powerlessness” (Khemani 2005) of local governments may undermine the willingness and ability of citizens to monitor their performance and to hold them accountable in elections. First, when local governments are financed by central transfers, rather than from local sources, citizens may lack *incentives* to monitor how public money is spent (Faguet 2008). Second, under partial decentralization, they may also lack *information* about the expenditure responsibilities of local governments and about the amount of funds available for service provision in their localities (Khemani 2005; Gadenne 2012; Joanis 2014). Third, when decentralization is partial, citizens may have low *expectations* of the role of local governments in providing local public goods and assign this responsibility to the central government (e.g., Devarajan et al. 2009). All this, in turn, may reduce the accountability of local officials to voters and create perverse incentives for them to engage in corruption and patronage spending, while blaming the central government for reduced public goods spending (Khemani 2005; Bardhan 2009).

Consistent with this, evidence from rural India (Devarajan et al. 2009) and Nigeria (Khemani 2005) suggests that, the less autonomy local governments have to raise their revenues and to allocate their budgets, the less likely they are to be – and to be perceived as being – effective, accountable and trustworthy. The unintended consequences of making decentralization partial are well described by Smoke (2003: 10):

Poorly articulated roles and resource deficiencies can cripple local governments and undermine incentives for local officials and elected representatives to perform effectively. Similarly, if local people participate in public decision-making and see no concrete result because local officials have inadequate power and resources to deliver services, they may become disillusioned and cynical about local government.

A second instance of “partial decentralization” is what Weingast (2009: 288) calls the “tragic brilliance” of one-party dominant regimes – or “how insecure governments use centralized fiscal control to undermine elections”. In this case, a centralized fiscal system weakens the accountability relationship between local governments and citizens, through its (negative) effects on *political competition* (Díaz-Cayeros et al. 2003; Weingast 2009, 2014).

In one-party dominant regimes where local governments are heavily dependent on discretionary transfers from the central government - such as, Mexico under the *Partido Revolucionario Institucional* (Institutional Revolutionary Party) (1930s-1990s) – the fiscal system provides a mechanism for the party in control of the central government to distribute transfers across localities selectively according to their political characteristics – whether they are governed by its own members or by the opposition. This has two consequences. First, it undermines the ability of opposition parties to govern effectively, as they systematically receive less transfers. Second, it undermines the incentives of citizens to vote for the opposition – regardless of how corrupt the dominant party is (Díaz-Cayeros et al. 2003; Weingast 2009, 2014).

In this case, the problem with “partial decentralization” is not that fiscal institutions create or exacerbate “political market imperfections”, such as information asymmetries between voters and officials (e.g., Ahmad et al. 2006), but rather that they make the “political market” much less contestable. In this case, local elections are not an imperfect mechanism of political accountability in the hands of voters, but rather an effective mechanism of political control in the hands of the national ruling party. This is explained by Weingast (2014: 20) as follows:

The tragic brilliance mechanism reveals a political motivation for why regimes in developing countries centralize policy and taxation authority in comparison with developed ones. Wholly apart from administrative efficiencies and fiscal equity, centralization affords insecure political regimes with political leverage over lower governments and citizens. By making the delivery of basic local public goods and services depend on whom citizens vote for, the incumbent regime at once restricts citizens ability to throw the rascals out, to exercise fiscal autonomy, and to influence public policies.

To summarize, the partial decentralization literature shows how the *power* relationship between the central and local governments affects the *accountability* relationship between local governments and citizens: when the central government does not devolve (fiscal) decision-making power to local governments, citizens are less able and willing to hold them accountable for the quality of the services provided in their localities. Under partial decentralization, central-local fiscal relations distort (local) state-society relations in various ways. In some cases, the (fiscal) powerlessness of local government results in high levels of political disengagement and an “accountability gap” between citizens and local officials. In others, the (fiscal) dependence of local governments on the central government gives way to what Fox (2000: 8) calls “reverse vertical accountability” – a situation in which “accountability flows more from society upwards than from the state downwards” (Khemani 2005, 2007a; Ahmad et al. 2006; Ahmad and Brosio 2009; Bardhan 2009; Devarajan et al. 2009; Lockwood 2009; Weingast 2009, 2014).

In China, village governments have become increasingly dependent on fiscal transfers from higher-level governments, particularly in agricultural regions. Changes in the way village governments are financed and in the autonomy with which they allocate public funds may fundamentally change the relationships of power and accountability between village governments, higher-level governments and villagers, and not necessarily in ways that improve village governance and public goods provision. The literature on partial decentralization suggests various channels through which the centralization of the fiscal system may have negatively affected the accountability role of village elections and the positive relationship between village democracy and public goods provision. First, fiscal reforms have sharply reduced the amount of resources over which village governments have control or discretion, limiting the scope of what they can do and be held accountable for. This raises the question of whether villagers still view and use elections as an accountability mechanism and whether there is a positive relationship between the degree of village democratization and the level of village-financed investment. Second, and relatedly, fiscal reforms have made village governments heavily reliant on (earmarked) transfers from higher-level governments to provide public goods. If county and township Party committees use the fiscal system for political purposes

and target more investment to villages that are governed by Party branches rather than by popularly elected village committees, there may be a negative relationship between the degree of village democratization and the amount of government-financed investment. These questions will be examined in the next chapter.

2.6. Summary

Is China one of the most decentralized countries in the world, or one of the most centralized? In fact, as noted by Bahl (2011: 247), it is both. This chapter has provided an overview of the processes of (expenditure) decentralization and (revenue) centralization that have shaped intergovernmental fiscal relations under the fiscal contracting system (1980-1993) and the tax-sharing system (1994-present), highlighting the growth of vertical fiscal imbalances at the local level, and the resulting dependence of local governments on central transfers, as one of the most important changes in local public finance in recent years. Both under the fiscal contracting system (1980-1993) and the tax-sharing system (1994-present), local governments have accounted for more than 70 percent of total government expenditures (i.e., high degree of expenditure decentralization). However, the introduction of the tax-sharing system (1994) led to a “drastic” recentralization of revenues (Wong 2009), increasing the central share from around 20 to 60 percent of the total (Fock and Wong 2008). The recentralization of (enterprise and individual) income taxes (2002-03), the elimination of rural fees (2000-04) and agricultural taxes (2004-06), and the implementation of the “New Socialist Countryside” program to improve rural services (2006 – present) have further eroded the revenue base of local governments, while increasing their reliance on transfers to finance the provision of services, especially in rural areas (e.g., Tian 2009). Today, transfers absorb around 60 percent of central revenues and finance between 40 and 50 percent of local expenditures (i.e., high degree of revenue centralization) (Wong 2010, 2011; Whiting 2011). In the comparative federalism literature, China emerges less as an example of “market-preserving federalism” (e.g., Weingast 2009) than as an “outlier” in terms of vertical imbalance and transfer dependency (e.g., Bahl 2011; Fock and Wong 2008). At the same time, the intergovernmental transfer system still scores very

poorly in terms of efficiency, equity and transparency (e.g., Qiao and Shah 2006; Wong 2007ab, 2010, 2011).

Previous studies show that fiscal institutions – the intergovernmental fiscal system and interjurisdictional competition – have largely failed to provide grassroots governments with either sufficient *fiscal resources*, or adequate *fiscal incentives*, to meet the needs of rural residents for public services (e.g., West and Wong 1995; World Bank 2002; Duckett 2007; Murphy 2007; Tsai 2007ab; Wong 2007ab, 2009, 2010, 2011; Fock and Wong 2008; Saich 2008). They also suggest that rural tax reforms may have aggravated these problems (e.g., Takeuchi 2014; Chen 2015). A question that has yet to be fully answered is whether and in what ways the (fiscal) dependence of villages on higher-level governments makes village officials less (politically) accountable to villagers for the provision of public goods.

Studies looking at the political aspects of fiscal decentralization warn against the risk of reducing local fiscal autonomy as a way to prevent local corruption, because it might actually reduce local political accountability, by making decentralization “partial” (e.g., Ahmad and Brosio 2009; Devarajan et al. 2009; Bardhan 2009). When local governments are heavily dependent on transfers from the central government, there tend to be higher levels of government corruption and lower levels of political trust and participation at the local level (Fisman and Gatti 2002; De Mello 2004; Khemani 2005; Fan et al. 2009). One of the main reasons is that citizens are less able and willing to hold local governments accountable for how they use transfer revenues than tax revenues (Faguet 2008; Gadenne 2012). Thus, the less autonomy local governments have to raise their revenues and to allocate their budgets, the less likely they are to be – and to be perceived as being – accountable and trustworthy (e.g., Smoke 2003; Khemani 2005; Devarajan et al. 2009). At the same time, the less accountable and trustworthy local governments are – or are perceived to be –, the greater the challenges that they will face to elicit compliance and participation from citizens in the areas of tax collection and service provision (e.g., Fjeldstad and Semboja 2001; Smoke 2011). In sum, central-local (fiscal) relations may affect local state-society relations in ways that undermine the (political) incentives of local officials and local citizens to work together for the public good.

According to Oates (1999: 1143), fiscal reform efforts in the developing world should focus on “restructuring systems of intergovernmental grants, in some instances to reduce the extent of financing that they provide to local governments, and, more generally, to remove the perverse incentives that they often embody for fiscal behaviour on the part of recipients”. He further argues that “the case for establishing adequate and effective tax systems at decentralized levels of government is one of the critical issues of fiscal federalism in the developing world”. China is no exception. Like in other developing countries, where the Tiebout model (Tiebout 1956) has not provided solutions to the problem of poor rural service provision, in China interjurisdictional competition has not allowed rural residents to use the “exit” option (i.e., migration) to either prevent predatory taxation and/or to have their demands for public services met. The question now is whether the recentralization of the intergovernmental fiscal system has also left them without the option to exercise “voice” in the governance of their communities. This is examined in the next chapter.

Chapter 3
Political Institutions and the Provision of Local Public Goods

3.1 Introduction

What are the potential and limits of local democratic reforms as a means to improve government accountability and public goods provision in a non-democratic regime like China? There is little consensus in the empirical literature on whether village committee elections provide an effective mechanism for village residents to hold grassroots officials accountable for the quality of the public goods and services provided in their communities (Zhang et al. 2004; Luo et al. 2007, 2010; Tsai 2007ab; Wang and Yao 2007; Sato 2008; Kung et al. 2009; Martinez-Bravo et al. 2011; Meng and Zhang 2011; Mu and Zhang 2014; Lu 2015). A possible limitation of existing studies, however, is that, in their analysis of the relationship between grassroots political reforms and public goods provision, they do not examine whether changes in “the access to power” resulting from the introduction of village elections have been matched by changes in the “exercise of power” (O’Brien and Han 2009) or, in other words, whether democratically elected village committees have been given the power to govern. An often implicit assumption is that decisions about investment in village infrastructure are made at the village level, and are made by village committees.

There are, however, reasons to think that the balance of power (i.e., control over fiscal resources) is increasingly tilted towards Party organizations at the county, township and village levels. For instance, some studies show that, in poorer communities, village officials “routinely” go to the county to “lobby for additional public investments for their villages” (Mu and Zhang 2014: 19) and that, in the implementation of public projects funded by higher-level governments, they merely “execute orders or guidelines passed down from above” (Ahlers and Schubert 2009: 57). Others indicate that, in richer villages, Party organizations are still the “locus of power” and have full control over village finances (Oi and Rozelle 2000; Zhang et al. 2004; Sun et al. 2013). To the extent that villages rely on their own funds to invest in basic infrastructure, it is often village Party secretaries, not village committee heads, the ones who decide whether and in what to invest. This suggests that, regardless of whether village-level public projects are funded by village or higher-level governments, village committees often have no say in the provision of public goods. To the extent that this is the case, an analysis of the determinants of government performance at the village level that focuses on the accountability

relations between village committees and voters without simultaneously examining the power relations between village committees and other state and party actors risks missing the forest for the trees. Likewise, since village committees are likely to be relegated to a subordinate position vis-à-vis township and village Party organizations, an exclusive focus on the incentive effects of village committee elections does not address the issue of how the Party's accountability mechanisms (e.g., cadre responsibility system and intra-Party elections) shape the incentives of township and village Party officials (i.e., the most likely power-holders) to implement democratic reforms and to invest in public goods in village communities.

The overall goal of this chapter is to examine the institutional determinants of government spending on public goods at the village level. We pursue two interrelated objectives. The first one is to assess the impact of village democracy on village public goods provision, and the second one to examine the effects of the cadre responsibility system and intra-Party elections on village democratization and village public goods provision. By "village democracy" we mean a governance system in which village committees are elected in (reasonably) free and fair elections, and have the power to (co-)manage local affairs (with village Party branches). We use the term "village public goods provision" to refer to (capital and current) spending on infrastructure by village governments. In rural China, village infrastructure projects (e.g., roads, bridges, irrigation, drainage, drinking water, and schools) are typically financed either by village governments from current revenues, savings or debt, or by higher-level governments through grants. Our analysis focuses on explaining inter-village differences in the level of infrastructure investment *made* by village governments (i.e., village-financed investment). The question of what explains differences among villages in the amount of infrastructure investment *received from* higher-level governments will also be explored (i.e., government-financed investment).

Our main goal is to find out whether and under which conditions village committee elections matter for government accountability and public goods provision. We argue that this might depend on: (i) who finances village public projects – higher-level governments or the village – and (ii) who controls village finances – the Party branch and/or the village committee. If elections do not provide

citizens with a means to influence and monitor how public funds are used in their communities, either because fiscal resources have been centralized and the spending autonomy of village governments reduced and/or because, despite the introduction of elections, political power still lies outside popularly elected institutions, they are unlikely to improve local governance and public goods provision. In the context of rural China, we argue that, to the extent that public spending decisions are made either by county and township governments (i.e., village infrastructure projects funded by higher-level governments) or by village Party branches (i.e., village infrastructure projects funded by the village), village elections are unlikely to enhance the accountability of public spending.

Given the dominant role of township and village Party officials in village governance, in this chapter we also explore the impact of the cadre responsibility system and village Party branch elections on village public goods provision and village democracy. These political institutions represent key mechanisms of (bureaucratic and democratic) accountability within the Party – between the top officials at the village level (i.e., the village committee head and village Party secretary) and the Party committee at the township level, in the case of the cadre responsibility system; and between the village Party secretary and village Party members, in the case of Party branch elections (Whiting 2001; 2006; Edin 2003ab; Tsui and Wang 2004; Tsai 2007b; Ong 2012; Sun et al. 2013).

The cadre responsibility system lies at the core of China's governing system. Unlike in a rule of law system, in China's "rule of mandates" system, higher-level officials hold lower-level officials accountable, not for the implementation of the country's laws and policies, but for the implementation of a subset of "mandates", that is, a subset of "directives that are hierarchically ranked against each other" (Birney 2014: 55). They do so through the use of performance contracts, which include a list of targets ranked according to their importance (i.e., "priority targets with veto power", "hard targets" and "soft targets"), and provide various incentives to lower-level officials for their fulfilment (Birney 2014: 55).

Existing studies on the cadre responsibility system show that it has largely failed to create (career and financial) incentives for township and village officials to improve the quality of village elections (Kennedy 2007b; Sun et al. 2013; Birney

2014) and public goods provision (Tsai 2007b). They argue that county and township officials have been unwilling and unable to hold lower-level officials accountable for their performance in these policy areas (Kennedy 2007b; Tsai 2007b; Birney 2014), and point to three reasons (Tsai 2007b: 232-240). First, although performance contracts generally include targets related to social development and political decentralization, these tend to be categorized as “soft targets” (Kennedy 2007b; Tsai 2007b), whose fulfilment is neither sufficient nor even necessary for grassroots cadres to advance in their careers. Second, higher-level governments have little (fiscal and political) leverage over village governments, mainly as a result of the small share of transfers in village budgets, and the lack of promotion opportunities for village cadres within the local Party-state (Tsai 2007b). And, third, higher-level officials often lack accurate and reliable information about the performance of their subordinates at lower levels of the administrative hierarchy (Birney 2014; Tsai 2007b).

The picture of the cadre responsibility system that emerges from these studies is thus a bleak one. At best, this mechanism of top-down control, is “selectively effective” (Edin 2003a), in that it induces local officials to implement what their Party superiors consider to be high-priority policies (i.e., “priority targets with veto power” and “hard targets”) but to ignore the rest (i.e., “soft targets”) (O’Brien and Li 1999; Whiting 2001; 2006; Edin 2003ab; Kennedy 2007b; Birney 2014). At worst, it is unable to solve agency problems between the different levels of the Party-state and to make grassroots officials (e.g., village committee head and village Party secretary) accountable to higher-level Party leaders (e.g., township Party secretary) (Bernstein and Lü 2003; Tsai 2007b). This picture, however, may have changed, at least in part, as a result of the recentralization of the fiscal and administrative systems in recent years. Of particular significance is the adoption of the “salaries-from-above” and “cadre-in-residence” policies (Smith 2010; Oi et al. 2012), which are likely to have enhanced the leverage of higher-level officials over village cadres, while reducing the degree of information asymmetry between them. According to the “salaries-from-above” policy, the salaries of the main officials at the village level are to be paid by county or township governments from funds transferred by the central government, and not by villagers through fees. Under the cadre-in-residence policy, townships are,

in turn, required to assign a township official to each of their villages, so as to ensure that they have more and better information about the performance of village cadres (Oi et al. 2012: 656). These policies may mitigate agency problems between village officials and township cadres. However, the question is whether they will not exacerbate agency problems between village officials and villagers. This may partly depend on whether higher-level officials and villagers have the same priorities or not. In this chapter, we explore the impact of the cadre responsibility system on village public goods provision and village democracy. Based on the literature, it is hypothesized that, while the cadre responsibility system may or may not positively affect the provision of local public goods, it is unlikely to exert a positive effect on the implementation of village democratic reforms.

Unlike in the case of the cadre responsibility system, there is very little research on the impact of intra-Party democratic reforms on rural governance. Another objective of this chapter is to provide a preliminary assessment of both the effects of intra-Party democracy on village public goods provision, and its interaction with village-level democracy. In recent years, the central government has encouraged the introduction of elections for village Party branches (i.e., “two-ballot system”), as well as the merger of the positions of village committee head and Party branch secretary (i.e., *yijiantiao* system) (Guo and Bernstein 2004; He 2007; O’Brien and Han 2009; Huang and Chen 2010; Chan 2007; Sun et al. 2013). Case study evidence suggests that intra-Party democratic reforms may improve public goods provision in village communities, either (i) by making Party leaders (downwardly) accountable to Party members for the management of village funds (e.g., intra-Party elections) (Li 1999) or (ii) by reducing the number of village cadres and the level of village administrative costs (e.g., concurrent office-holding) (Guo and Bernstein 2004). However, on the other hand, they may undermine village democracy in the longer term by (i) reinforcing the balance of power in favour of village Party organizations and against village committees (Sun et al. 2013) (e.g., intra-Party elections) or by (ii) blurring the boundaries between government and Party institutions and eliminating the new system of checks and balances created by the Organic Law of Village Committees (e.g., concurrent office-holding) (He 2007; Schubert and Ahlers 2012a). Since intra-Party democratic reforms may affect village governance and public goods

provision through different channels, we examine the effects of “intra-Party elections” and “concurrent-office holding” separately, paying particular attention to whether township Party committees interfere in the election of village Party secretaries. This would weaken their electoral accountability to village Party members (in the case of intra-Party elections) or all villagers (in the case of concurrent office-holding). The underlying intuition is that the way in which intra-Party democratic reforms are carried out may affect their outcomes and, more specifically, the likelihood that they complement, rather than subvert, local democratic reforms and improve public goods provision.

The chapter is structured as follows. In section 3.2 we analyze the distribution of resources and authority among levels of governments, and between non-Party and Party institutions at the grassroots level. We do so by examining (i) who invests in village-level infrastructure (i.e., the village or higher levels of government), and (ii) who manages village-level funds (i.e., the village committee or the Party branch). Section 3.3 undertakes a review of the relevant literature and develops hypotheses regarding: (i) the effects of village committee elections, the cadre responsibility system and intra-Party elections on village public goods provision (i.e., village-financed investment); and (ii) the interaction among these political institutions. In Sections 3.4 and 3.5 we develop and estimate a two-equation simultaneous equation system, in which “village democracy” and “village public goods provision” (i.e., village-financed investment) are the endogenous variables (i.e., main model). Additionally, and for comparison purposes, we develop and estimate a two-equation simultaneous equation system, in which “village democracy” and “government-financed investment” are the endogenous variables (i.e., additional model). Section 3.6 summarizes our findings and concludes.

3.2 Power, Accountability and State Provision of Infrastructure

In the 11th and 12th Five-Year Plans (2006-2010 and 2011-2015), the central government has expressed its commitment to “strengthen rural infrastructure and public services” (Zhang et al. 2013: 87-88)⁴¹. To reach this goal, it has adopted a more centralized approach to governing rural areas, one that relies primarily on: (i) using (mostly, earmarked) grants to finance rural governments (e.g., Fock and Wong 2008); strengthening the (upward) accountability of township and county governments to the provincial and central governments (e.g., Heberer and Trappel 2013); (ii) limiting the autonomy and decision-making power of village officials (e.g., Oi et al. 2012); (iii) reinforcing the dominant role of the Party in managing village affairs (e.g., Alpermann 2013); and promoting democracy, not in villages, but especially within rural grassroots Party organizations (“intra-Party democracy”) (e.g., Brown 2011).

While there is wide agreement about the main challenges to further improve the provision of rural infrastructure - the weak fiscal capacity and political accountability of rural governments - (e.g., World Bank 2007), it is not entirely clear that these reforms are moving in the right direction. Questions have been raised about whether relying on earmarked grants and top-down control can improve the quality of governance and public goods provision in rural communities (e.g., Wong 2010; Bird et al. 2011; Oi et al. 2012), especially without undertaking a fundamental reform of the fiscal and administrative systems (World Bank 2007; Fock and Wong 2008). For instance, Richard Bird and colleagues argue that “the development of more responsive and sustainable local fiscal management in China will inevitably require both the devolution of more decision-making power over public finance to local governments and the development of local governments that are more openly and directly responsible to the local people whom they are supposed to serve” (Bird et al. 2011: 242).

A main concern with the new government’s approach to improving rural public goods provision is that, under the new (de-)centralized system, village

⁴¹Between 2006 and 2012, it invested more than 6 trillion yuan in rural infrastructure and, partly thanks to this investment, 95 percent of the country’s villages have now access to paved roads, running water, and electricity (Anderlini 2012).

committees have less control over fiscal resources, and villagers have less control over how they are spent. And yet, village committees are the only political institutions that can be held democratically accountable for their spending decisions, while villagers are the ones with first-hand information on the infrastructure needed and provided in their communities. By shifting resources and authority away from village committees towards higher-level governments and grassroots Party organizations, these new central policies may render village committee elections useless as a mechanism of control and thereby widen the “accountability gap” at the grassroots level. A fundamental question is, therefore, who makes decisions about infrastructure investment in village communities? And what implications may this have for accountability in infrastructure delivery?

An analysis of the distribution of power among different levels of the Party-state, and between the Party and the state, warns us against assuming that village committees and those they represent have a voice in local investment decisions. One reason has to do with the vertical distribution of power between levels of government and the degree of fiscal autonomy of villages. Recent fiscal reforms have limited the discretionary authority of villages to determine the level and composition of their expenditures, by restricting their revenue-raising capacity, while making them heavily dependent on specific-purpose transfers from higher-level governments – transfers that are distributed across villages on an *ad hoc* basis, rather than according to objective criteria (Fock and Wong 2008; Ahlers and Schubert 2009; Tan 2010; Bird et al. 2011; Oi et al. 2012; Boyle et al 2014). This has affected how villages and higher-level governments interact, reducing the autonomy of villages in the financing and provision of infrastructure⁴².

The introduction of the tax-sharing system (1994), the implementation of the tax-for-fee reform (2002-04), and the abolition of agricultural taxes (2004-06) have limited the capacity of villages to finance public projects from their own resources (Bird et al. 2011; Oi et al. 2012). Research by Bird et al. (2011), amongst others (e.g.,

⁴² Since the early 1980s, village governments had been responsible for financing and providing small-scale infrastructure in their communities, such as roads and bridges, irrigation and drinking water systems, or schools and clinics (Tsai 2007b: 31-35). The revenue used to build and repair village-level infrastructure used to come from various tax and non-tax sources (e.g., agricultural taxes, village fees or *tiliu*, and profits from village enterprises) (Tsai 2007b; Boyle et al. 2014; Mu and Zhang 2014).

Luo et al. 2007, 2010; Zhang et al. 2007; Yi et al. 2011; Boyle et al. 2014), shows a dramatic change in the sources of investment in village infrastructure – including, roads and bridges, irrigation and drinking water systems, or schools and clinics –, especially after the implementation of the tax-for-fee reform (2002-04). As can be seen in Table 3.1, between 2000 and 2004, the share of village-level public investment financed by higher-level governments almost tripled, increasing from 21 to 59 percent (Bird et al. 2011). The picture emerging from our data also reveals the increased dependence of villages on (earmarked) transfers to finance their capital expenditures since 2002⁴³. Table 3.2 shows that, in 2003-04, more than 50 percent of total infrastructure investment in our sample villages came from higher-level governments. More recent survey research has found that the share of village-level investment funded by (earmarked) transfers continued to increase after the abolition of agricultural taxes, reaching around 75 percent in 2008 (Oi et al. 2012). This share is even higher in poor villages, where investments made by higher-level governments have replaced, rather than complemented, their own investments (Bird et al. 2011; Oi et al. 2012).

Table 3.1: Proportion of investment in village public projects financed by higher-level governments before and after the tax-for-fee reform

Public goods investment per capita	2000		2004	
	Mean	Percent from higher levels	Mean	Percent from higher levels
Roads and bridges	15.1	23.4	123.6	64.8
Schools	8.9	23.8	7.3	30.9
Irrigation	10.2	42.3	20.4	50.5
Drinking water	4.3	4.6	17.6	42.7
Clinic	0.0	0.0	0.9	0.0
Other ^b	9.8	1.2	21.6	61.3
Total investment	48.4	21.3	191.3	59.2

Source: Bird et al. (2011: 235)

Notes: ^bOther includes electricity, village office building construction, green for grain projects, and investments in communications, etc.

⁴³ This reflects the impact of the tax-for-fee reform, which eliminated village fees (e.g., tiliu) and capped the amount of voluntary contributions from villagers for village public projects (i.e., the “yi shi yi yi” system) (e.g., Luo et al. 2007; Yi et al. 2011; Boyle et al. 2014).

Table 3.2: Variation in sources of funding for village public projects

Province	Total value of investment from higher levels (yuan)		Share of investment from higher levels (%)	
	Mean	SD	Mean	SD
Jiangsu	328.70	280.51	62.90	31.67
Sichuan	344.84	321.99	54.05	28.03
Shaanxi	71.65	104.97	55.80	46.50
Jilin	118.75	149.08	50.50	40.47
Hebei	59.90	115.78	36.99	44.87
Fujian	260.59	294.59	61.29	35.54
Sample	201.15	255.96	54.29	37.28

Source: CCAP Village Survey (2005)

Changes in the way village-level infrastructure is financed have been accompanied by changes in the way projects are carried out. Villages have little, if any, say over the selection, design and implementation of infrastructure projects funded by higher-level governments (Ahlers and Schubert 2009; Tan 2010; Bird et al. 2011; Oi et al. 2012; Schubert and Ahlers 2012b)⁴⁴.

Another reason why village committees may have no control over fiscal resources has to do with the horizontal distribution of power between state and party institutions at the grassroots level. As discussed in section 1.3, the 2010 Organic Law of Village Committees, like the 1987 and 1998 versions of the Law, does not establish a clear division of powers between village committees and village Party branches. At the same time it underlines the “leading role” of Party organizations in local governance. One of the implications is that, even when local spending decisions are made at the village level, they are often made by Party branches. Table 3.3 shows the distribution of power between village committees and village Party organizations in our sample villages. In a majority of them, the decision-making power over how

⁴⁴ In some cases, villages do not even have a say over the management of the services provided by that infrastructure. For instance, in villages where most investment in irrigation infrastructure comes from the county and township governments, county and township-level water resource bureaus have taken on the responsibility of managing village irrigation systems (e.g., setting and collection of irrigation fees; signing of canal management contracts; etc.) (Boyle et al. 2014).

to spend their own revenues was concentrated in the hands of village Party leaders, who cannot be held electorally accountable by village residents. This finding is in line with those of previous studies (Zhang et al. 2004; Sun et al. 2013) and suggests that, despite almost three decades of “village self-government”, the nature of the local power structure has changed little: perhaps unsurprisingly, it is still completely dominated by the Party in most villages.

Table 3.3: Distribution of power over the allocation of village funds

% Villages by Province	(1) Village Party branch (secretary), the only decision-making body (person). Village leader cannot be held electorally accountable by villagers	(2) Village committee (head), granted decision-making power. Village leader can be held electorally accountable by villagers ⁴⁵
Fujian	45%	55%
Hebei	42%	58%
Jiangsu	53%	47%
Jilin	67%	33%
Shaanxi	56%	44%
Sichuan	65%	35%
Sample	55%	45%

Source: CCAP Village Survey (2005)

Previous studies on the relationship between village committee elections and public goods provision have not simultaneously examined how changes in the intergovernmental fiscal arena and the lack of change in the local political arena have jointly affected the ability of village elections to generate accountability in the post-tax-for-fee reform period. They generally fail to capture either the recentralization of the fiscal system (e.g., Zhang et al. 2004; Tsai 2007b; Wang and Yao 2007; Shen and Yao 2008) or the continued leadership of Party organizations in rural communities (e.g., Luo et al. 2007, 2010; Sato 2008; Meng and Zhang 2011). However, the effects of village democracy on the provision of village infrastructure may crucially depend on whether village committees have control over the allocation of resources and, in

⁴⁵ Around sixteen percent of the sample villages have merged the positions of village Party secretary and village committee head. As will be explained in detail in section 3.4.1, we establish a distinction between villages with a unitary power structure, in which (1) the village leader was chosen through competitive village elections with an open nomination process (i.e., the “haixuan” or sea-election method), and those in which (2) the posts of village committee head and Party secretary have been merged but the village leader is not directly nominated and elected by all villagers.

particular, on: (i) who funds village public goods projects – whether higher-level governments and/or villages themselves – and (ii) who manages village funds – whether the Party branch and/or the village committee. If village committees lack resources and power - either as a result of their fiscal dependence on (earmarked) transfers from higher-level governments or their political subordination to village Party branches –, villagers will have neither the means nor the incentive to use village elections as an accountability mechanism. Consistent with this, it has been found that inter-village variation in voter turnout is partly explained by (i) the level of own revenues of villages (Su et al. 2011); and (ii) the type of power-sharing arrangements between the (elected) village committee head and the (unelected) village Party secretary (Zhong and Chen 2002): the greater the fiscal autonomy and political power of (elected) village committees, the higher the turnout. In sum, in a majority of rural communities elected village committees have little control over resources and, therefore, little power to govern, which in turn might have negative implications for the functioning of village democratic institutions.

Although more research is needed, the available evidence suggests that shifting the responsibility for funding village infrastructure projects to higher-level governments and/or to village Party branches does not necessarily increase the (productive and allocative) efficiency of village-level capital expenditures - whether funded from above or by the village. A first issue is the accountability of grant-financed expenditures. Existing studies show that, under the new intergovernmental transfer system, the central government has limited control over how earmarked grants are actually allocated and spent by rural officials, and so do villagers (World Bank 2007; Fock and Wong 2008; Liu M. et al. 2009). It seems that the lack of transparency of a system dominated by a “multitude of *ad hoc* earmarked grants” (Dollar and Hofman 2008) has increased opportunities for corruption and collusion among local officials at the county, township and village levels, while leaving villagers in the dark (Ahlers and Schubert 2009). This lack of accountability in the distribution and use of grant funds might explain: (i) why villages with political connections to higher-level governments (i.e., *guanxi*) receive more transfers for infrastructure projects (Zhang et al. 2007; Luo et al. 2007, 2010; Boyle et al. 2014) but tend to have poorer quality infrastructure than other villages (Liu C. et al 2009);

as well as (ii) why inter-village variation in the proportion of village households satisfied with infrastructure provision is largely explained by inter-village variation in the sources of public investment (i.e., higher-level governments or villages themselves): the higher the share of investment financed by higher-level governments through grants, the lower the level of satisfaction among villagers with the infrastructure provided (Bird et al. 2011). A second issue that deserves attention is the accountability of self-financed expenditures. In this regard, it has been found that the concentration of power in the hands of appointed village Party secretaries is associated with a less efficient use of village funds and with a poorer provision of village infrastructure. In communities where elected village committees have no decision-making power, a smaller share of the budget goes to infrastructure construction and maintenance (Zhang et al. 2004), while their roads, drinking water systems and irrigation networks are of significantly lower quality than those of other villages (Liu C. et al. 2009).

Three basic conclusions can be drawn from this discussion. First, making rural governments more accountable to villagers for the provision of local public goods remains a crucial issue. Second, village elections seem a necessary component of the accountability framework for rural service provision that the central government is attempting to build. Third, the main obstacle to electoral accountability is not – or not only – whether villagers have control over village committees, but more fundamentally whether village committees have control over fiscal resources.

3.3 Hypotheses Development

3.3.1 Village Democracy

In China, political decentralization reforms have only been implemented at the village level, and have been implemented unevenly across villages. Inter-village variation in the degree of political decentralization is mainly associated with inter-village variation in the procedural and substantive dimensions of grassroots

democracy: (i) the quality of village committee elections, and (ii) the autonomy and authority of village committees to govern (O'Brien and Zhao 2011).

To date, research on the development of village democracy has been mainly focused on the first of these dimensions. There is a large body of literature examining the determinants and effects of "high-quality elections" (Lu 2012). These studies suggest that the quality of elections has improved more on paper than in practice; that it is undermined by old and new forms of electoral manipulation and corruption; and that it varies widely across stages of the electoral process, as well as villages (Tsai 2007b: 203-209; O'Brien and Han 2009: 363-367; Kennedy 2010b; Su et al. 2011; Lu 2012: 487-488). For instance, a nationally representative survey of more than 350 villages in 27 provinces has found that only 16 percent of villages conducted their last election in full accordance with the Organic Law of Village Committees (Lu 2012). Another survey of more than 300 villages in Shanxi, Hebei, Jiangxi and Fujian suggests that pre-election and election procedures vary in the degree to which they are effectively implemented. Some of the rules and procedures mandated by the Organic Law - such as "multiple candidates" (98 % of villages), "campaign speeches" (54%) "secret ballot booths" (77%), "public vote count" (87%) or "immediate announcement of election results" (99%) - are implemented in most villages. And yet others are largely ignored: fifty-nine percent of villages reported that in their last election there was interference from the township government, the village Party branch or the incumbent village committee in the formation of the village election committee and the selection of candidates ("pre-election procedures"); sixty percent that they did not regulate proxy voting ("regulated proxy voting"); and seventy percent that they used mobile ballot boxes ("fixed ballot boxes") (Tsai 2007b: 203-209). While "old" challenges to improving the quality of village elections, such as township interference in candidate nomination, have yet to be addressed, "new" problems associated with the use of proxy voting and mobile ballot boxes, such as vote-buying and voter intimidation, have arisen (e.g., O'Brien and Han 2009; Kennedy 2010b). Although these problems are relatively common, elections are not everywhere equally corruptible or corrupt: villages vary widely in their electoral institutions and practices. As Kennedy (2010a: 169) has pointed out,

“the quality of grassroots political reform varies throughout rural China from fair elections to electoral manipulation”.

What explains inter-village variation in election quality? The literature suggests that the explanation lies in the economic, political and social contexts in which village committee elections are embedded, and in the ways in which they shape electoral competition and participation. One strand of the literature examines the economic determinants of election quality (e.g., Lawrence 1994; O’Brien 1994; Choate 1997; Epstein 1997; Shi 1999; Oi and Rozelle 2000; Hu 2005; He 2007; Zweig and Fung 2007). Among these studies, there is agreement that the level and pattern of local economic development matters, but there is less agreement as to which villages are more likely to have better electoral institutions and practices: rich (e.g., Hu 2005; He 2007; O’Brien 1994), middle-income (e.g. Epstein 1997; Shi 1999; Zweig and Fung 2007; Schubert and Ahlers 2012a), or poor villages (e.g., Choate 1997; Lawrence 1994); those with an agriculture-dependent (e.g., Oi and Rozelle 2000) or diversified economy (e.g., He 2007); those with a tradition of (local) state (e.g., O’Brien 1994) or private entrepreneurship (e.g., Oi and Rozelle 2000); those with more (e.g., Hu 2005) or less (out-)migration (e.g., Oi and Rozelle 2000; Lu 2012).

For instance, according to Kevin O’Brien (1994: 48), elections are more likely to be better implemented in rich villages with a large number of collective enterprises, where “cadres have a large public sector to administer and to profit from (as well as a reduced concern with electoral removal and humiliation) and peasants have an interest in ensuring that public funds are not misused or squandered”. In contrast, Jean Oi and Scott Rozelle (2000: 529) argue that the incidence of contested elections is likely to be higher in poorer, agricultural villages with little out-migration, where “villagers have an incentive to participate in politics and leaders do not have an incentive to limit such activities”, as they do not fear the loss of control over revenue-generation activities (e.g., collective enterprises). Tianjian Shi (1999: 439-440), in turn, argues that middle-income communities, where village committees derive most of their revenues from local taxes and fees, are more likely to have competitive elections. This is because in villages where local officials need to “ask for money” from villagers, the latter are more likely to “ask for the right to

participate” in village governance. Despite their differences, what these studies have in common is that they examine how economic factors shape what Kennedy (2010a) calls the “supply” and “demand” for grassroots democratic reforms. By examining the economic interests of the main political actors at the village level, they show: (i) how the dependence of village residents on village resources for their income (e.g., land and village-owned enterprises) affects their incentives to participate in village politics, as a means of influencing the way in which such resources are distributed and managed; and (ii) how the access of village leaders to non-tax incomes (e.g., enterprise profits, land rentals, etc.) affects both their incentives to open up the local political arena to participation, and their ability to “buy off” village residents.

A second strand of the literature argues that the main obstacles for improving election quality lie in the local political arena. “Village electoral democracy” is constrained by two interrelated problems: the manipulation of village elections by Party officials and the declining political participation of villagers (e.g., Kelliher 1997; Alpermann 2001; Ogden 2002; Zhong and Chen 2002; He 2007; Tan and Xin 2007; O’Brien and Han 2009; Kennedy 2010a; Landry et al. 2010; Tao et al. 2011; Schubert and Ahlers 2012a). With the introduction of elections for village committees, township and village Party officials have seen their power reduced and their legitimacy contested. It has made it more difficult for township leaders to elicit the necessary cooperation from village officials to implement unpopular tasks, whose fulfilment is nonetheless critically important for a good performance evaluation from county leaders under the target responsibility system (e.g., O’Brien and Li 1999; Huang and Chen 2010). It has also made it more difficult for village Party secretaries to maintain their position as “the undisputed boss of the village” (*yibashou*) (Guo and Bernstein 2004). They thus have a strong incentive to interfere in elections and influence their outcomes, so long as this does not lead to violent protests from villagers that draw attention from higher-level governments (Louie 2001; He 2007; Kennedy 2007b; Huang and Chen 2010; Tao et al. 2011). Research conducted by Kennedy (2007b: 63) shows that in villages where village committee elections are rigged “the village committees have relatively weak authority to govern, and villagers have few mechanisms to monitor or influence cadre behavior”. In these villages, there are also low levels of political trust and voter turnout: in the view of

villagers, the costs of participating in elections - whether as voters or candidates - outweigh the potential benefits (Zhong and Chen 2002; Landry et al 2010; Tao et al. 2011).

A third line of research examines the ways in which features of the social structure and context affect the quality of elections. Much of this literature focuses on the (re-)emergence of traditional and new social groups – in particular, clan organizations and private entrepreneurs -, and on the possible risk that village democracy is undermined by problems of clientelism and elite capture (e.g., Dickson 2008; Levy 2003, 2007; Hu 2008; Yao 2012; Wang 2014). The re-emergence of clans in rural areas after decades of repression under Mao has provided a basis for “identity politics” (Brown 2011; Su et al. 2011; Mu and Zhang 2014), manifested in practices of clan-based voting and patronage which distort patterns of electoral participation and competition. In this regard, it has been found that in villages where a few clans vie for power, voter turnout is higher, but clan-based voting is prevalent (Su et al. 2011). For instance, there is evidence that “one needs to belong to a big lineage in order to be elected”, and that “no matter how incompetent a candidate is (...) close members of his lineage will vote for him” (Hu 2008: 624). It has also been found that, in order to gain electoral support, both incumbents and their challengers often build clientelistic ties with fellow clan members, by offering – or promising to offer - “small favors” with public funds (Hu 2008: 624)⁴⁶. Regardless of their apparent quality, elections in these communities are unlikely to deliver better governance because “lineage votes” (*jiazu piao*) (Hu 2008) serve neither to select capable leaders nor to discipline corrupt ones, but to signal loyalty to the clan group and to secure access to publicly provided private goods.

The development of the rural private sector and the emergence of private entrepreneurs also seems to have created more challenges than opportunities for village democracy (Levy 2003, 2007; He 2007; Huang and Chen 2010; Yao 2012). While the introduction of elections has provided a means by which “a new, more economically based rural elite” can challenge “the older political elite” (Levy 2007: 21), the question is whether this is to the benefit of ordinary villagers. Some studies

⁴⁶ This may explain the finding that villager satisfaction with elections in multi-surname villages tends to be lower than in single-surname villages (Kennedy 2002).

argue that private entrepreneurs' entry into the electoral arena and power structure is key to increasing political competition and bringing about political change (e.g., Oi and Rozelle 2000; He 2007). Put succinctly, "no new rich, no true competition, therefore no village democracy" (He 2007: 165). However, others show that private entrepreneurs' entry into village politics has in fact been associated with growing problems of vote-buying and corruption (e.g., Levy 2003, 2007; Kennedy 2010b; Yao 2012). In much the same way as clan-based voting, vote-buying distorts electoral competition and participation, undermining the ability of village elections to deliver what villagers demand, that is, "financially clean and public-minded" leaders (Yao 2012). Underlying these issues is the broader question of social inequality and the ways in which it weakens the accountability role of elections: Who sells her/his vote? Who does not vote? Whose interests are not represented? (e.g., poorer villagers, minority clan members, migrant workers, women, etc.). The problem in this case is that, in villages where part of the population does not - or cannot - use the vote to select better leaders and to hold them accountable for their performance⁴⁷, elections merely provide a mechanism for replacing the old local elite with a new one, but not for constraining in any meaningful way how this new elite exercises power. In some communities, villagers complain that "elections only produce many more greedy cadres, and each new generation is worse than the previous one" (Hu 2008: 624).

What are the implications of inter-village variation in election quality for local public finances and public goods provision? The existing literature does not provide a conclusive answer to this question. Some studies offer evidence that the introduction of direct elections for village committees is positively associated with both lower taxation and higher public goods spending (e.g., Bernstein and Lü 2003; Zhang et al. 2004; Luo et al. 2007, 2010; Sato 2008; Shen and Yao 2008; Kung et al. 2009). In villages where leaders are directly elected by villagers, tax collection is characterized by "greater fairness and less abuse" (Bernstein and Lü 2003: 224). Furthermore, villagers pay less taxes, but do not receive less or lower-quality services

⁴⁷ For instance, survey research on village elections in Henan and Shandong reveals that, in 15 percent of the surveyed villages, around one-third of the villagers were de facto disenfranchised from voting in village committee elections, with some of the reasons being: "only the men vote", "only party members vote", "only one member of each household can vote" or "I was never informed that there was an election" (Birney 2014: 59).

(Zhang et al. 2004). Indeed, elected village officials invest more on roads, schools, medical care, drinking water and irrigation systems (Luo et al 2007, 2010; Shen and Yao 2008; Kung et al. 2009) and provide better infrastructure (Liu C. et al. 2009). The reason is that, along with the change from appointed to elected villages heads, there has been a shift in taxation from households to collective enterprises (Zhang et al. 2004), as well as a reduction in corruption (e.g., embezzlement of village funds) and wasteful spending (e.g., “entertainment” expenses, such as “wining and dining”) (Bernstein and Lü 2003). One possible interpretation of these findings is that, as a result of elections, the fiscal relationship between grassroots governments and villagers has gradually moved towards the “contractual” end of the continuum between “coercive” and “contractual” taxation (Moore 2008: 37), where there is an “exchange” of taxes for services between them.

In contrast to these studies, others call into question the usefulness of elections to improve government accountability - no matter how (well) they are implemented (Tsai 2007ab; Meng and Zhang 2011; Mu and Zhang 2014). They suggest that differences among villages in the quality of their “pre-election institutions” (Tsai 2007b) (i.e., the determination of the members of the village election committee and the election candidates) are not associated with differences in the composition of their spending (Tsai 2007ab; Meng and Zhang 2011), or not in the way one would expect (Wang and Yao 2007). For instance, findings by Wang and Yao (2007) show that in villages with government-controlled elections, where candidates are nominated by local officials, a larger share of the budget goes to the provision of basic infrastructure (e.g., roads, irrigation, school and clinic projects) and social welfare (e.g., transfers to households), as compared to villages with competitive elections, where candidates are nominated by villagers. Inter-village variation in the quality of “election institutions” does not seem to matter either. Research conducted by Tsai (2007b: 187-227) shows that villages that conduct their elections in (greater) accordance with the established rules and procedures – including, “contested elections”, “public vote count”, “secret ballot booths”, “campaign speeches”, “regulated proxy voting”, “fixed ballot boxes”, and “immediate announcement of election results” - do not invest more in public projects, nor do they provide their constituents with better drinking water, roads or schools.

These studies argue that “democratic institutions are neither necessary nor sufficient for governmental accountability and responsible provision of public goods” (Tsai 2007b:203).

What explains this lack of consensus in the empirical literature? A possible reason has to do with the challenge of assessing and measuring local democracy, especially in an authoritarian regime. In fact, it has been pointed out that one of the main limitations of recent research on (political) decentralization in developing countries is that it has been dominated by “a concern with the substantive dimension of democracy rather than the process dimension of democracy” (Packel 2008: 1). This does not hold, however, for the literature on (political) decentralization in China. Indeed, we find the opposite problem: existing studies on the relationship between local democracy and public goods provision have focused on the “process” dimension of democracy – the freedom and fairness of village committee elections – , rather than on its “substantive” dimension – the autonomy and authority of village committees to govern. Despite these differences, and irrespective of their regional focus, there is a similar imperative among studies on decentralized governance to adopt a broader definition of local democracy that encompasses its main dimensions. In the case of China, this is more challenging and yet more important, given the Party’s traditional monopoly over the allocation of political power at each level of the administrative hierarchy (Landry 2008). The adoption of a two-dimensional definition of “village democracy” (i.e., “process” and “substantive” democracy), while still minimalist, may help us find an answer to the puzzle of why existing studies on village committee elections have come to such different conclusions about their effects, and to the question of why villages with better elections fail to deliver better governance. Our main hypothesis is that, in villages where elections are better implemented, and where village committees have decision-making power over the allocation of village funds, there will be higher levels of investment in public goods (i.e., village-financed investment).

3.3.2 Intra-Party Democracy

In recent years the Chinese Communist Party has begun to promote “intra-Party democracy” at the grassroots level, through the introduction of a new system of “intra-party elections” and “concurrent office-holding” in the villages (Li 1999; Schubert 2003; Guo and Bernstein 2004; Chan 2007; He 2007; Alpermann 2010, 2013; Sun et al. 2013). These reforms are best understood in the context of the continuing competition for “power” and “legitimacy” between (elected) village committees and (appointed) village Party branches (O’Brien and Han 2009). Traditionally, these two governing bodies have derived their authority from different sources and exercised it in different ways. Unlike popularly elected village heads, village Party secretaries are typically appointed by township Party committees and, consequently, tend to be more responsive to the demands of their Party superiors than to the needs of villagers (Guo and Bernstein 2004; Bernstein 2006; He 2007; Tan and Xin 2007; Huang and Chen 2010).

The gradual institutionalization of village committee elections has created challenges for village Party branches, and by extension for townships, to maintain their dominant role in village governance. The main reason lies in their lack of democratic legitimacy. By creating an “electoral connection” (Manion 1996) between villagers and village heads, the regular holding of democratic elections has provided the latter with the incentive and justification, not only to resist township interference in village affairs, but also to compete with (appointed) Party secretaries for village leadership (Schubert 2003; Guo and Bernstein 2004; He 2007; Alpermann 2010, 2013; Sun et al. 2013). In villages with well-run elections, village committees enjoy more popular support than Party branches (Guo and Bernstein 2004: 258), and a majority of villagers consider that they should have a greater say in the management of village affairs because, unlike Party organizations, they represent them (Tan and Xin 2007: 592-593). In these villages, there are growing conflicts between village committees, on the one hand, and village and township Party organizations, on the other (Li 1999; Schubert 2003; Guo and Bernstein 2004; Bernstein 2006; He 2007; Tan and Xin 2007; Landry 2008; Huang and Chen 2010).

More “intra-party democracy” has been the response given to the unanticipated, and unwelcome, effects of “village democracy” and, in particular, to

what Schubert (2003) calls the “horizontalisation of power relations” among community, state and party actors. In his view, “the Party is trying to secure its monopoly power by gradually introducing more transparency and democratic procedures to intra-party decision-making concerning the recruitment of local office-holders” (Schubert 2003: 5). The introduction of elections for village Party branches and the merger of Party branches and village committees can be seen as a step in this direction. In an increasing number of villages, Party branch secretaries are no longer appointed by the township, but elected by and among the village Party members, through the two-ballot system – a two-stage electoral process in which villagers first nominate the candidates for the Party secretary position, and Party members then elect their leader from among the nominated candidates. Likewise, in some provinces, such as Guangdong, it is increasingly common that the positions of village Party secretary and village head are held by the same person. Either the incumbent Party secretary is required to run in village committee elections, or the newly elected village head is first recruited into the Party, and subsequently promoted to the position of village Party secretary (Guo and Bernstein 2004; Chan 2007; He 2007; O’Brien and Han 2009; Huang and Chen 2010; Sun et al. 2013).

What these reforms – intra-Party elections and concurrent office-holding - have in common is their objective of making village Party secretaries democratically accountable, either to Party members (intra-Party elections) or to all villagers (concurrent office-holding) (Schubert 2003; Guo and Bernstein 2004; Chan 2007; He 2007; Sun et al. 2013). However, they differ in terms of: (i) the type of institutional change they involve – the introduction of new (democratic) mechanisms of accountability within the Party (intra-Party elections) or, alternatively, the merger of Party and non-Party institutions at the grassroots level (concurrent office-holding) – ; and (ii) the type of power structure they create – a dual or a single village power structure.

The implementation of intra-Party democratic reforms might affect the provision of local public goods and the development of local democracy in different ways and through different channels. As previously pointed out, there is case study evidence showing that they may help to improve public goods provision by (i) increasing Party accountability (e.g., intra-Party elections) (Li 1999) or by (ii)

reducing administrative expenses in village budgets (e.g., concurrent office-holding) (Guo and Bernstein 2004). At the same time, there are also concerns that they may undermine village democracy by (i) reinforcing the power of village Party branches (e.g., intra-Party elections) (Sun et al. 2013) or by (ii) eliminating village committees as a separate and relatively independent political institution (e.g., concurrent office-holding) (He 2007; O'Brien and Han 2009; Schubert and Ahlers 2012a). The main underlying question is whether intra-Party democratic reforms have the potential of opening Party institutions to popular participation (Chan 1998), or, rather, the objective of subjecting government institutions (and those they represent) to greater Party control (O'Brien and Han 2009). This might depend on the type of reform implemented and the way it is implemented.

In this respect, some studies argue that the introduction of elections for village Party branches may be more likely to improve public goods provision and less likely to undermine village democracy than concurrent office-holding (“*yijiantiao*” or “two posts on one shoulder”), mainly because it does not lead to a concentration of power in one person’s hands (Li 1999; Schubert and Ahlers 2012a; Sun et al. 2013). Other studies (Guo and Bernstein 2004), however, argue that, by requiring village Party secretaries to run in elections – whether intra-Party elections or village committee elections in the case of concurrent office-holding – both types of reforms are equally likely to give community members the opportunity to hold village Party secretaries accountable⁴⁸ for their performance, as long as elections are free and fair. Hence, irrespective of the form that intra-Party democratic reforms take, the key issue is whether they are implemented in a way that makes village Party secretaries (electorally) accountable and, in particular, whether they prevent township Party committees from interfering in the (s)election of village Party secretaries (Guo and Bernstein 2004). In line with this latter view, our basic hypothesis is that any of these reforms is more likely to improve the provision of public goods, and less likely to undermine village-level democracy, if village Party secretaries are elected either by village Party members or by all villagers (i.e., intra-Party or popular election),

⁴⁸ Research conducted by Guo and Bernstein (2004: 272) on the adoption of the *yijiantiao* model in Guangdong province found that, “when elections were free and fair, the requirement that a Party secretary had to win the electoral competition for village committee office probably did serve as an incentive for him/her to be more responsive to the interests of the constituents”.

without undue interference from township officials in the candidate nomination process, a stage of the electoral process which is particularly vulnerable to manipulation.

3.3.3 Bureaucratic Control

Defined as “a system of targets and incentives that control local cadres and influence which policies and laws they implement” (Birney 2014: 56), the cadre responsibility system is a central component of China’s political system. It has provided the Party with a means to monitor and influence the behaviour of local officials and, ultimately, to maintain (political) control over the process of (economic) decentralization (Whiting 2001, 2006; Edin 2003ab; Tsui and Wang 2004; Heimer 2006; Kennedy 2007b; Tsai 2007b; Landry 2008; Gao 2009; Ong 2012; Birney 2014). There is agreement in the literature, however, that its implementation has resulted in neither better service provision (Tsai 2007), nor more democratic governance in rural areas (Kennedy 2007b; Sun et al. 2013; Birney 2014). This has been attributed to two main causes: the relatively low priority of these issues on the central policy agenda and the ineffectiveness of the cadre responsibility system as a mechanism of political accountability (Kennedy 2007b; Tsai 2007b; Birney 2014).

The first possible reason why the cadre responsibility system has not had a positive impact on the functioning of village democratic institutions and the provision of village public goods has to do with what grassroots cadres are held accountable for by higher-level governments. Under this system, Party committees at each level of the administrative hierarchy (e.g., county Party committee) use performance contracts to assign tasks and objectives to the top officials at the next lower level (e.g., township head and township Party secretary) and to establish a direct link between their subordinates’ performance, on the one hand, and their salary and promotion, on the other. Yet not all targets and tasks are equally important or given the same priority: they are hierarchically ranked according to their importance from “priority targets with veto power” and “hard targets” to “soft targets” (Ong 2012: 465).

One of the main shortcomings of the cadre responsibility system is that it provides lower-level officials with both the incentive and the opportunity to ignore or even hinder the implementation of low-priority policies (i.e., “soft targets”). This is for three reasons. First, under the cadre responsibility system, what “makes or breaks” a career within the local Party-state is the fulfilment of the high-priority tasks included in performance contracts (i.e., “priority” and “hard” targets) (Ong 2012: 465). Second, while local officials are required and expected to implement high-priority policies (i.e., “priority” and “hard” targets), they are allowed to “adjust” the implementation of low-priority tasks (i.e., “soft” targets) to that end (Birney 2014: 55). And, third, high- and low-priority policies often compete for government resources and/or have conflicting goals (Whiting 2006; Birney 2014).

One of the consequences is that the cadre responsibility system has failed to create incentives for township and village officials to improve the quality of service provision (Tsai 2007b) and local democracy (O’Brien and Li 1999; Kennedy 2007b; Sun et al. 2013; Birney 2014). Under the cadre responsibility system, lower-level officials can safely ignore demands from higher-level officials to invest more in public goods or to interfere less in village politics. This is because performance contracts with higher-level officials do not prioritize and, in some cases, do not even include goals related to the delivery of public goods or the promotion of grassroots democracy (O’Brien and Li 1999; Whiting 2001, 2006; Edin 2003ab; Kennedy 2007b; Tsai 2007b; Birney 2014). For instance, research conducted by Ong (2012) in Zhejiang, Shandong and Hebei provinces (see Table 3.4) shows how township officials are required by county Party leaders to focus their efforts and resources on implementing the one-child policy (“priority target”), preserving social stability (“priority target”), generating fiscal revenues (“hard target”), or promoting rural industry (“hard target”), rather than on improving education and healthcare provision or implementing the Organic Law of Village Committees.

Table 3.4: Cadre-Evaluation Criteria in Three Townships

	Township A	Township B	Township D
Province	Zhejiang	Shandong	Hebei
Basic economic indicators			
Income per capita (Yuan)	7079	5000	2800
GDP ratio			
Primary (%)	21.4	35.0	40.5
Secondary (%)	50.6	48.0	18.0
Tertiary (%)	28.0	17.0	41.5
Cadre-evaluation criteria			
Priority targets with veto power	<ul style="list-style-type: none"> • Population control • Social stability • Petition cases 	<ul style="list-style-type: none"> • Population control • Workplace safety 	<ul style="list-style-type: none"> • Population control • Social stability • Petition cases
Hard targets	<ul style="list-style-type: none"> • Fiscal revenue • Industrial production • Amount of investment attracted • Number of large industrial enterprises • Number of industrial parks 	<ul style="list-style-type: none"> • Fiscal revenue • Industrial production • Amount of investment attracted 	<ul style="list-style-type: none"> • Fiscal revenue • Industrial production • Farmers' income
Soft targets	<ul style="list-style-type: none"> • Farmers' income • Education and healthcare provision • Grassroots organization development • Cultural and social development 	<ul style="list-style-type: none"> • Size of private economy • Farmers' income • Education and healthcare provision • Social stability • Petition cases • Grassroots organization development • Cultural and social development 	<ul style="list-style-type: none"> • Amount of investment attracted • Agricultural development • Forestry conservation • Cultural and social development

Source: Adapted from Ong (2012: 466).

Another of the consequences of the implementation of the cadre responsibility system is that it actually creates perverse incentives for lower-level officials to underinvest in local public goods and to thwart local democratic reforms (i.e., low-priority policies), albeit for different reasons. A first problem is that performance contracts or, rather, the way in which they are used allows and encourages the diversion of fiscal and human resources away from rural service provision in various ways. One way is by focusing local officials' attention on "revenue generation" and "short-term economic growth" (Whiting 2006: 7). Years ago, there was little to discourage grassroots cadres from investing in the development of collective enterprises (Tsai 2007b: 46). And now there is little to discourage them from investing in the development of industrial parks and development zones (Whiting 2011), despite questions then and now about the effectiveness and sustainability of these local development strategies, especially in poor regions (e.g., Park et al. 1996; Liu et al. 2008). Another way in which the cadre responsibility system diverts resources away from service provision is by requiring village officials to spend much of their budget and time on completing unpopular "state tasks", such as implementing the one-child policy, instead of carrying out "community tasks", such as providing public services or mediating disputes among village residents (O'Brien and Li 1999; Tsui and Wang 2004; Tan and Xin 2007; Kung et al. 2009; Smith 2010). For instance, in their survey of more than 1,000 villagers in a dozen villages of Anhui province, Tan and Xin (2007: 589-590) found that a majority of them believe that village cadres prioritize carrying out the tasks handed down by the township government, rather than providing public services to their communities. In sum, whether by inducing local governments to behave as revenue maximizers (e.g., Whiting 2006) or as service providers for county and township leaders (e.g., Smith 2010), the use of performance contracts to hold grassroots cadres accountable for implementing high-priority policies has reduced the resources available for meeting service demands from villagers, while increasing spending on revenue-generating activities and administrative costs.

A second problem related to the perverse incentives embedded in the cadre responsibility system is not that low- and high-priority policies compete for resources, but rather that they have competing or conflicting objectives (Gao 2009;

Whiting 2011; Birney 2014). The goals of low-priority policies, such as the implementation of village democratic reforms, may either conflict with the *goals* of policies designated as high priority or with the *strategies* used to implement them. For instance, there is a clear conflict between the goal of promoting village democracy and the growing reliance of grassroots governments on illegal land grabs to generate tax and non-tax revenues (e.g., Birney 2014). More fundamentally, by removing the power of township officials to appoint and dismiss village officials (i.e., village committee head and members), village democratic reforms have weakened their authority over their former “subordinates” – the very same authority that they need to elicit their cooperation in meeting the high-priority targets set by county leaders in their performance contracts, especially when achieving such targets requires or justifies going against the interests of villagers (e.g., implementation of the one-child policy, expropriation of land, etc.) (e.g., Guo and Bernstein 2004; Martinez-Bravo et al. 2011; Sun et al. 2013).

To sum up, one argument about why the use of performance contracts by higher-level Party officials has not had a positive impact on village governance and rural service provision is because these are not seen as high-priority policy areas by the central government. And, at the same time, under the cadre responsibility system, lower-level officials have an incentive to avoid the implementation of policies that fall in this category. From this perspective, one of the main limitations of China’s “rule of mandates system” is that it creates “a precise but narrow space of accountability” (Birney 2014: 56): under the cadre responsibility system, local officials can be held accountable for enforcing policies that rank high on the central government agenda - nothing more, nothing less.

A different argument for why the cadre responsibility system has failed to make grassroots officials accountable for the provision of local services and the implementation of local democratic reforms is that the centre is unable to elicit compliance from its local agents on these and other issues (e.g., Bernstein and Lü 2003; Chen 2007; Tsai 2007b). Some studies argue that, during much of the reform period, there has been a problem of “inadequate state capacity” (Bernstein and Lu 2003: 84) that has mainly resulted from a “vertical deconcentration of power”. The incentive and monitoring mechanisms intended to reduce agency problems between

different levels of the Party-state have been weakened by the process of fiscal and administrative decentralization that has taken place since the early 1980s (Bernstein and Lü 2003; Chen 2007; Tsai 2007b).

First, by requiring each level of the Party-state to finance its own expenditures, including their cadres' salaries, fiscal decentralization reforms have eliminated the possibility of using intergovernmental transfers, not only as a mechanism of fiscal redistribution, but also as a mechanism of political control (Tsai 2007b: 232-234). Second, administrative decentralization reforms have weakened the bureaucratic monitoring system. The cadre responsibility system does not provide the central government with an effective mechanism to obtain reliable and accurate information about what goes on at the grassroots level (Wedeman 2001; Tsai 2007b). Information about the activities and performance of village and township governments is subject to distortion: first, because they report on themselves; second, because this information is not directly reported to the central government, but instead passes from one level of government to the next before it reaches Beijing; and, third, because higher-level officials have incentives to turn a blind eye to misreporting by lower-level officials, in so far as it helps them meet their own performance targets, at least on paper if not in practice (Tsai 2007b: 238-243)⁴⁹. Hence, from this perspective, local governance problems have their origin in a weak central government that lacks the monitoring and incentive mechanisms required to hold rural governments to account.

This second argument – that the ineffectiveness of the cadre responsibility system is indicative more of a lack of government capacity than of a lack of government will – seems less compelling today than years ago. The main reason is that it fails to take account of the changes that have taken place in the fiscal and administrative structures of the state. Reforms aimed at (re-)centralizing fiscal resources and administrative control – such as the introduction of the tax-sharing system or the adoption of the “salaries-from-above” and “cadre-in-residence” policies – should have provided higher-level governments and, ultimately, the central

⁴⁹ The bureaucracies created to monitor and audit local governments – the General Auditing Administration and the Ministry of Supervision – have been decentralized, which has led to the paradoxical situation in which their staff at local levels are appointed and paid by the very same local government agencies they are required to supervise (Huang 1996; Tsai 2007b; Chien 2010).

government with new means to incentivize and monitor the performance of rural officials, especially at the township and village levels (Oi et al. 2012). Not only do village governments depend heavily on transfers under the new intergovernmental fiscal system, but also the leading village officials are now paid and more closely monitored by township and county governments. There is anecdotal evidence that village officials complain about the presence of “sent-down cadres” in their villages as an “infringement of the village’s sphere of self-governance” (Smith 2010: 614), and that they fear having their salaries withheld by township cadres for not implementing some of their mandates or directives (Oi et al. 2012: 257). Other reforms adopted by the central government in order to recruit and maintain “capable” village officials - such as increasing their salaries and improving their promotion opportunities – (Kung et al. 2009: 74) should also have given higher-level officials greater leverage over village cadres. The fact that village officials were rarely promoted to higher levels was seen as one of the reasons for the limited effectiveness of the cadre responsibility system at the village level (Chen 2007: 157; Tsai 2007b: 235)⁵⁰. However, the fact that the central government now encourages “selecting civil servants from among village cadres” (Kung et al. 2009: 74) implies that this might no longer be the case.

Overall, this discussion suggests that agency problems between the centre and the localities may be less severe now than in the recent past, if only because higher levels have more – and seemingly more effective - means to elicit compliance from lower levels. Consequently, the question may not be so much whether but, rather, how the cadre responsibility system shapes the behaviour of township and village officials. This brings us back to the question with which we started: what are grassroots officials held accountable for? Are township officials held to account by their Party superiors for promoting village democratic reforms? Do they hold village officials accountable for investing in public goods?

⁵⁰ Until recently, a regulation passed in 1996 stipulating that “rural civil servants (i.e., government officials) must not be selected directly from among incumbent village cadres” limited the career advancement opportunities for village cadres (Chen 2007: 157).

Based on the literature, we hypothesize that, while the cadre responsibility system may or may not have a positive impact on village public goods provision, it is unlikely to exert a positive effect on the implementation of village democratic reforms. Improving rural infrastructure and services has moved up on the policy agenda, especially after Hu Jintao and Wen Jiabao came to power. Since 2003, every “Number One Central Document”⁵¹ has focused on rural issues, including rural service provision (World Bank 2007; Michelson 2012). Also since 2006, improving rural infrastructure and services has been a core component of “the New Socialist Countryside” programme (World Bank 2007; Schubert and Ahlers 2011, 2012b). However, recent studies suggest that after the rural tax reform, performance contracts with village officials still do not prioritize public goods provision (Chen 2015). On the other hand, the central government has not shown a strong commitment to push forward the implementation of village democratic reforms in recent years. Instead, it has increasingly emphasized the role of the cadre responsibility system and intra-Party democratic reforms in increasing the accountability of rural officials to higher-level officials and grassroots Party members (Whiting 2006; Chan 2007).

3.4 Variables, Econometric Model and Estimation Method

To address our research questions, we develop a two-equation simultaneous equation model of “village democracy” and “village public goods provision” and estimate it using three-stage least squares (3SLS). “Village democracy” is defined as a governance system in which village committees are elected in (reasonably) free and fair elections, and have the power to (co-)manage local affairs (with village Party branches). “Village public goods provision” refers to capital and current spending on infrastructure by village governments.

As discussed in section 1.4, our choice of econometric model is driven by two main considerations. The first one is the likely reverse causality between village democracy and village public goods provision. In villages governed by

⁵¹ This is a key policy document issued by the State Council and the Party Central Committee at the beginning of each year to outline the priorities of the central government.

democratically elected village committees, village heads might have stronger incentives to invest in infrastructure in order to remain in office, while villagers might have stronger incentives to participate in village politics (e.g., village committee elections, village representative assemblies, etc.) in order to influence and control how public funds are spent and what public goods are provided⁵². Village democracy might affect and be affected by village public goods provision.

A second consideration is that this model also allows us to include measures of the implementation of intra-Party elections and the cadre responsibility system as exogenous variables in each of the equations and to examine their impact on village-level democratization and public goods provision. The assumption that these variables are exogenous to the system seems reasonable, given that decisions regarding both the method for (s)electing village Party secretaries, as well the terms of their performance contracts are made by county and township leaders.

Additionally, we estimate a two-equation simultaneous equation system, in which “village democracy” and “government-financed investment” are the endogenous variables. In this case, we use the share of village investment financed by higher-level governments as the main dependent variable. This allows us to explore two questions: (i) whether county and township Party committees target resources to villages where the Party branch remains the dominant governing body; and (ii) whether this tends to undermine the demand for and implementation of grassroots democratic reforms.

Finally, to estimate both models, we use three-stage least squares for two reasons: (i) using system estimation methods is more efficient than using single-equation estimation methods; and (ii) 3SLS is the most commonly used system estimation method (Wooldridge 2006: 567). In the remainder of the section, we define the key variables included in the main model and provide descriptive statistics

⁵² There is evidence that elected and appointed village leaders face different incentives to improve public goods provision: investing in roads, irrigation and schools increases the probability of being re-elected, but not of being re-appointed (Luo et al. 2010: 678-680). Likewise, there is evidence that villagers in different localities face different incentives to participate in elections. According to He (2007: 81-84), the “value” of elections is one of the most important determinants of voter turnout: in villages where elections have not helped to reduced corruption and to improve service delivery participation levels are significantly lower.

of the main variables. We also explain how we address the identification problem in order to be able to estimate the two-equation models by 3SLS.

3.4.1 Village Democracy and Village Public Goods Provision

The first dependent variable in the model is “village public goods provision”, which refers to village spending on infrastructure. As can be seen in Table 3.5, there is great variation among the villages in the sample in terms of the level of funds allocated to the provision of basic infrastructures, such as roads, irrigation and drinking water systems or school buildings. Per capita spending on infrastructure (2003-04) varied from RMB 0 to RMB 1,374, with an average of RMB 134.85 and a standard deviation of RMB 208.45. Villages in Sichuan recorded the highest level of infrastructure spending (193.21 yuan per capita), and villages in Hebei the lowest (68.67 yuan per capita) during 2003-04.

Table 3.5: Variation in village government expenditures on infrastructure (in yuan)

Province	Per capita expenditure on infrastructure construction	Per capita expenditure on infrastructure maintenance	Per capita expenditure on infrastructure construction and maintenance (2003-04)	
	Mean	Mean	Mean	Std. Dev.
Jiangsu	156.86	18.26	175.12	185.10
Sichuan	188.16	5.05	193.21	150.59
Shaanxi	112.61	3.93	116.54	320.26
Jilin	81.72	9.15	90.87	107.66
Hebei	66.04	2.62	68.66	111.60
Fujian	144.48	17.47	161.95	286.30
Sample	125.27	9.58	134.85	208.45

Source: CCAP Village Survey (2005)

The measure of village public goods provision used in the main model is the log of per capita village government expenditure on infrastructure in 2003-04. This approach to measuring village public goods provision is consistent with recent findings in the literature. They suggest that, in order to explain inter-village differences in public goods investment, we need to distinguish between “subsidized investments” and “own investments”, because “each source of investment has its own determinants” (Zhang et al. 2007: 126-131). The characteristics of villages that make them more likely to receive investments from higher-level governments are not necessarily the same as those that make them more willing and able to invest in themselves. For instance, while higher-level governments may not necessarily target more investment to more democratic villages, more democratic villages may be able to mobilize more resources for infrastructure projects from villagers, due to the greater accountability and legitimacy of their leaders. Actually, evidence from the irrigation sector shows that in communities where elected village committees, rather than townships or village Party branches, have decision-making authority over irrigation matters, there are higher levels of (cash and labour) contributions from farmers to build or repair their irrigation systems, because “they are more confident that they will be able to capture the benefits of their investments” (Boyle et al. 2014: 15). Using a measure of village public goods provision that captures the share of spending over which villages have effective control or full discretion might better reflect inter-village differences in the quality of their governance systems and in the accountability (or lack thereof) of their leaders. What we want to find out is whether democratically elected village committees are more responsive to local needs in the allocation of village funds when given the power to govern. Additionally, we will explore the question of whether more democratic villages receive more or less transfers from higher-level governments.

“Village democracy” is the second dependent variable in the model. As pointed out in section 3.3.1, a possible limitation of existing studies on the relationship between local democracy and local public goods provision in rural China is that they focus on the “process” dimension of democracy – the freedom and fairness of village committee elections -, while paying insufficient attention to its “substantive” dimension – the power of village committees to govern. We thus

propose an alternative measure of village democracy: a single variable that captures inter-village variation in: (i) the quality of village committee elections; and (ii) the decision-making power of elected village committees. We construct a variable, called “village democracy index” (0-5), which is the product of: (i) an “election quality index” measuring the democratic quality of village committee elections (0-5); and (ii) a “power index” measuring the distribution of political power in the village (0-1). This measure of grassroots democracy, the village democracy index, allows us to quantify inter-village variation in the degree of political decentralization.

Assessing the quality of “authoritarian elections” (Landry et al. 2010) poses significant analytical challenges. There is, however, agreement that the freedom and fairness of Chinese village committee elections can be evaluated on the basis of “whether voters are free and have real choices in nominating candidates and voting for their choices by secret ballots”, and “whether electoral rules and procedures are administered free of violation, interference and fraudulence by village election committees” (Tan and Xin 2007: 582). Taking this into account, we develop an “election quality index” which incorporates information on the three most critical aspects or stages of the electoral process: how election committees⁵³ were formed – whether their members were selected by villagers (coded 1) or local officials (coded 0); how candidates were nominated – whether they were directly nominated by voters in open primaries (i.e., *haixuan* or “sea elections” method) (coded 1) or through other procedures (coded 0); and how votes were cast – whether secretly (coded 1) or publicly (coded 0); whether in person (coded 1) or by proxy (coded 0); and whether at a polling station (coded 1) or at roving ballot boxes (coded 0). We create a dichotomous variable for each of these election rules and procedures, which takes on the value of 1 if the village reported that it was duly implemented in the last election, and the value of 0 otherwise. We then combine these five variables into an additive index, the election quality index, which measures the democratic quality of the processes by which election oversight committees were formed, candidates nominated, and ballots cast in each of the sample villages. The election quality index scores range between 0 and 5, with higher scores denoting freer and fairer elections, in which: (1) election committee members were selected by villagers; (2) candidates

⁵³ Village election committees are responsible for organizing and overseeing the electoral process.

were directly nominated by voters through the *haixuan* system (i.e., open primaries); (3) secret voting booths were used; (4) proxy-voting was not allowed; and (5) roving ballot boxes were not used.

While these electoral practices are widely regarded as a *conditio sine qua non* in order to reduce opportunities for electoral manipulation and corruption (e.g., voter coercion, ballot box stuffing, vote buying, etc.) the survey data shows that some of them are still relatively uncommon in a majority of villages (see Table 3.6). For instance, the percentage of villages that in their last election used secret voting booths and banned proxy voting was as low as 11 percent and 35 percent, respectively⁵⁴. As can be seen in Table 3.6, of the 115 villages surveyed, only 2 conducted their last election in full accordance with these five basic electoral rules and procedures. This finding is in line with those of other recent studies (e.g., Tsai 2007b; Lu 2012) and reflects the poor governance of Chinese village committee elections more than fifteen years after the enactment of the 1998 Organic Law of Village Committees.

Table 3.6: Distribution of villages by level of election quality

Election Quality Index Score	No. Villages	Percent	Province	Mean	Std. Dev.
0	5	4.4	Jiangsu	2.84	1.21
1	18	15.7	Sichuan	2.15	0.93
2	30	26.1	Shaanxi	2	0.89
3	35	30.4	Jilin	3.48	1.03
4	25	21.7	Hebei	2.42	1.02
5	2	1.7	Fujian	2.25	1.29
Sample	115	100	Sample	2.55	1.17

Source: CCAP Village Survey (2005)

A more fundamental problem, however, might be that democratically elected village committees are as powerless now as they were in the late 1990s. In addition to the “election quality index”, we create a dichotomous variable, called “power

⁵⁴ Villagers participated in the selection of village election committee members and of candidates in 69 percent and 89 percent of the sample villages, respectively. 51 percent of the villages reported not having used roving ballot boxes in their last election.

index” that captures the nature of the village power structure and whether those who govern are subject to popular electoral control. In particular, this index takes the value of 1 when (i) villages have a dual power structure and the village committee (head) plays (at least) as important a role in determining the level and composition of village spending as the village party branch (secretary); or when (ii) villages have a unitary power structure – that is, the posts of village head and Party secretary have been merged (*yijiantiao*) – and the village leader was chosen through competitive village elections that had an open nomination process (i.e, the “haixuan” or sea-elections method). Alternatively, the village democracy index takes the value of 0 when (i) the village has a dual power structure but only the village Party branch (secretary) exercises authority over village finances and important village affairs; or (ii) the posts of village committee head and Party secretary have been merged but the village leader did not gain his/her position through “haixuan” elections, that is, s/he was not directly nominated and elected by all villagers⁵⁵.

Table 3.7 shows that in more than 80 percent of the sample villages there was a dual power structure, and in 50 percent all major decisions were made by the village Party branch (secretary) during the period of study. Around 27 percent of the villages were (co-)governed by village committees (with village Party branches). And only in 6 percent of them was the village committee head the main decision-maker in determining the use of village funds. Around 16 percent of the villages had introduced a new system of concurrent office-holding (i.e., *yijiantiao*)⁵⁶. However, their leaders were not subject to the same degree of electoral control. In this respect, we argue that it is necessary to establish a distinction between those villages where

⁵⁵ More specifically, the village democracy index takes on the value 1 if the village reported that: (a) the village committee is the leading governing body and has control over village finances; (b) the village committee head is the leading official and has control over village finances; (c) the village Party branch and the village committee share decision-making and implementation responsibilities and have an equally important say in the allocation of public funds; or (d) the posts of village committee head and village Party secretary are held by the same person (*yijiantiao*) and the village election followed the “haixuan” (sea-elections) method. Alternatively, it takes the value 0 if the village reported that: (a) the village committee is the leading governing body and has control over village finances; or (b) the posts of village committee head and Party secretary have been merged but the village leader did not gain his/her position through “haixuan” elections.

⁵⁶ As explained in section 3.3.2, this is typically done either by requiring the incumbent Party secretary – whether appointed by the township or elected by village Party members - to run in village committee elections or, if (s)he fails to be elected, by appointing the newly elected village committee head as the Party secretary.

the person serving concurrently as village head and Party secretary is required to pass the test of “haixuan” elections (11 percent of villages) – that is, village committee elections where villagers are entitled to freely nominate candidates - and those where s/he is not (5 percent). This is for three reasons. First, villagers who are not Party members can only hold village Party secretaries (electorally) accountable if the latter run for the position of village committee head (i.e., village committee elections). Second, it is more difficult for local officials to manipulate village committee elections when candidates are nominated by villagers (i.e., “haixuan” elections) than when they are nominated by the township government, the village Party branch or the incumbent village committee. Third, and relatedly, village committee elections are a (potentially) more effective mechanism of “downward” accountability than Party branch elections (He 2007).

For these reasons, the reform of merging the positions of village committee head and village Party secretary is likely to negatively affect village governance unless the village leader is made (electorally) accountable to the entire local population – and not only to Party members - through *haixuan* elections.

Table 3.7: Distribution of villages by type of power structure

Type of Power Structure	No. Villages	Percent
Power concentrated in village Party branch (secretary)	58	50.0
<i>Yijiantiao</i> (same person holds the positions of VC head and VPB secretary) – No “sea elections” (<i>haixuan</i>)	6	5.3
<i>Yijiantiao</i> (same person holds the positions of VC head and VPB secretary) – “Sea elections” (<i>haixuan</i>)	13	11.4
Power shared between village Party branch and village committee	31	27.2
Power concentrated in village committee (head)	7	6.1

Source: CCAP Village Survey (2005)

Reflecting the limited democratization of village governance, Table 3.8 shows that in the few villages where village committee elections were implemented in a reasonably free and fair manner, power has tended to remain concentrated in the hands of the village Party secretary. This confirms the concerns raised by O’Brien and Han (2009: 359) that “changes in the ‘exercise of power’ have not kept up with changes in the ‘access to power’”. The main reason is that village committees remain powerless even when – or especially when – they are democratically elected.

Table 3.8: Quality of elections and power of elected village committees

Election Quality Index Score	No. Villages	Less democratic power structure	More democratic power structure
0	5	2	3
1	18	13	5
2	30	19	11
3	35	15	20
4	25	12	13
5	2	2	0

Source: CCAP Village Survey (2005)

Finally, to quantify inter-village variation in the degree of political decentralization, we combine the “election quality index” and the “power index” into a single composite index, the “village democracy index”, which is calculated as the product of these two indices. Table 3.9 reports the mean and standard deviation of the values of the village democracy index in each of the sample provinces. It shows that the degree of political decentralization is low and varies considerably across villages and provinces: village democracy index scores range from 0 (58% of the villages) to 4 (11%), with a mean of 1.21. Villages in Jilin province provide the clearest example that the democratization of the village electoral process does not go hand in hand with the democratization of the village power structure: they have the highest “election quality” score (mean of 3.48) and one of the lowest “village democracy” scores (mean of 1.14), given that 67 percent of them are in fact not governed by popularly elected leaders.

Table 3.9: Village democracy index scores, by province

<i>Village Democracy Index Score</i>	No. Villages	Percent	<i>Province</i>	Mean	Std. Dev.
0	66	57.39	Jiangsu	1.58	1.77
1	5	4.35	Sichuan	0.75	1.25
2	11	9.57	Shaanxi	0.88	1.20
3	20	17.39	Jilin	1.14	1.71
4	13	11.30	Hebei	1.63	1.61
5	0	0	Fujian	1.25	1.52
Sample	115	100	Sample	1.21	1.54

Source: CCAP Village Survey (2005)

3.4.2 The Cadre Responsibility System

One of the main exogenous variables in the model is the cadre responsibility system, one of the main mechanisms of top-down control within the Party-state. We seek to assess its impact on village-level democracy and public goods provision. As discussed in section 3.3.3, county and township governments have now new means to influence and monitor the decisions and behaviour of (elected and unelected) village officials (e.g., “salaries-from-above” and “cadre-in-residence” policies): what they consider to be their priority tasks, how they divide them among themselves, and how they perform them. Hence, when examining the effects of the cadre responsibility system, the main question may not be so much whether, but how, it affects village governance structures and processes: whether, by increasing the influence of townships over village governance (i.e., who governs and how), it makes villages more or less democratically accountable to villagers, and village spending more or less responsive to public goods needs.

Our measure of the cadre responsibility system therefore needs to capture the extent to which village governance is shaped by higher-level governments. With this objective, we create a variable called “policy mandates index”, which measures the extent (%) to which the five top-priority tasks performed by village governments correspond to mandates or directives from township governments. Although this measure of bureaucratic control is a rough one, it gives an indication of the degree of

subordination and (upward) accountability of villages to townships. As can be seen in Table 3.10, the mean value of the index in our sample of villages is 82%, with a standard deviation of 18%. This finding indicates that higher-level governments exert tight control over village governments and raises the question of whether higher-level officials and villagers hold grassroots officials accountable for the same things.

Table 3.10: Policy mandates index scores, by province

Province	Policy Mandates Index (0-100)		
	No. Villages	Mean (%)	Std. Deviation
Jiangsu	19	85	15
Sichuan	20	96	10
Shaanxi	16	75	15
Jilin	21	80	18
Hebei	19	85	13
Fujian	20	73	25
Sample	115	82	18

Source: CCAP Village Survey (2005)

According to Kung et al. (2009), one of the effects of the cadre responsibility system is that village cadres “tend to give priority to state tasks first, seeing these as ‘hard responsibilities’, and they put community needs last”. They find that village officials allocate most of their time to (in descending order): “enforcement of the family-planning policy”; “organizing community agricultural production”; “addressing community members’ disputes”; “tax collection”; “community building”; and “receiving upper-level inspectors” (Kung et al. 2009: 66). County and township governments do not only influence how villages are governed, but also by whom they are governed. Findings by Sun et al. (2013) show that, the greater the dependence of township cadres on village officials to perform the tasks mandated by their county superiors, the lesser the likelihood that democratically elected village committees become the “locus of power” in villages.

3.4.3 Intra-Party Elections

The last institutional variable included in the model is village Party branch elections. To date, there has been very little research on this type of elections. One of the exceptions is the study conducted by Sun et al. (2013), the first one to provide a comprehensive analysis of how village Party secretaries are (s)elected and what this means for the distribution of power between Party branches and village committees. Their findings suggest that a minority of villages (48 percent) have introduced direct elections for village Party branches, in which Party members can directly nominate and elect the village Party secretary. Furthermore, an even smaller percentage of villages (13 percent) has implemented the so-called “two-ballot system” (Li 1999) and allowed all village residents, regardless of party membership, to participate in the nomination of candidates for the position of Party secretary (Sun et al. 2013: 12-14). These findings suggest that village Party branch elections are largely a top-down, intra-party affair.

The purpose of including this institutional variable in our model is to gain a preliminary understanding of how the new system of intra-Party elections might affect patterns of democratization and public goods spending at the village level. As pointed out by Alpermann (2010: 92), whether this reform can improve local governance may depend on whether it can effectively “break the hold of township party committees over village party secretary appointments”. Thus, following Sun et al. (2013: 12-13), we create a dummy variable “intra-Party election quality”, which captures the role of township Party officials in the (s)election of village Party secretaries. It takes the value 0 if the village Party secretary was selected by appointment, rather than by election, or if there was interference from the township in the electoral process, and the value 1 otherwise. Table 3.11 shows that, in 25 percent of the sample villages, Party secretaries were not democratically elected by Party members, either because there was no election and their Party secretaries were still directly appointed by the township (12 percent of villages) or because the township interfered in the electoral process, mainly through the nomination of candidates (7 percent). Sun et al. (2013) have found that the holding of competitive elections for village Party branches weakens village democracy by legitimizing the concentration of power in the hands of village Party secretaries. To our knowledge,

no previous study has examined the impact of village Party branch elections on village public goods provision.

Table 3.11: Township interference in the (s)election of village Party secretaries

Direct interference by the township in the (s)election of the village Party secretary	Total sample	Jiangsu	Sichuan	Shaanxi	Jilin	Hebei	Fujian
Yes (%)	25	32	40	38	5	32	5
No (%)	75	68	60	62	95	68	95
No. of villages	115	19	20	16	21	19	20

Source: CCAP Village Survey (2005)

3.4.4 Control Variables

To distinguish between the effects of institutional and non-institutional factors on village public goods provision, a number of economic, social, demographic and geographic variables are included in the model as controls. Our choice of control variables is based on the empirical literature on public goods provision in rural China (Zhang et al. 2004; Luo et al. 2007, 2010; Tsai 2007ab; Wang and Yao 2007; Sato 2008; Kung et al. 2009; Lu 2015).

First, we include a set of economic variables that capture inter-village variation in the level of economic development and the availability of resources for investing in public goods, namely: the log of per capita village government revenue; the log of per capita net income; the amount of per capita farmland (*mu*); the number of collective, private, and individual (*getihu*) enterprises; and the proportion of migrants in the village labour force. To avoid endogeneity bias, we use the 2000 values of these variables.

Second, to control for the effects of social structure and social divisions on public goods provision, the model includes measures of lineage structure and inter-lineage relations in the sample villages. A village's clan structure is measured by the proportion of households belonging to the three largest surname groups⁵⁷, that is, by

⁵⁷ This is in line with Manion (2006).

the degree of surname concentration. The nature of inter-clan relations is measured by a dummy variable, called inter-lineage tension index, which equals zero if relations between clans within a village are cooperative, and one if they are conflictual.

Finally, the model also controls for demographic and geographic differences among villages, including: the log of the village population; the proportion of village land that is flat; the share of cultivated land that is irrigated; the log of the distance from the township (km); and the provincial location (five provincial dummies excluding Jiangsu).

These three sets of control variables might affect the demand and supply of local public goods, as well as the cost of their provision. Previous studies have found that villages with a higher per capita income (e.g., Luo et al. 2007, 2010) and with more collective enterprises and self-employed households (*getihu*) (e.g., Zhang et al. 2004; Zhang et al. 2007; Luo et al. 2010) tend to invest more in public goods. This is in contrast to villages with a larger number of clan groups (e.g., Kung et al. 2009; Tsai 2007b) and out-migrants (e.g., Zhang et al. 2007; Luo et al. 2010), where there tends to be less investment. There is also evidence that villages with higher levels of revenue do not necessarily have higher levels of public goods spending (Tsai 2007b; Wang and Yao 2007), although this has been called into question by more recent studies (Kung et al. 2009).

3.4.5 Econometric Model and Estimation Method

To test the hypotheses put forward in section 3.3, a simultaneous equations model (SEM) of “village democracy” and “village public goods provision” is developed and estimated by three-stage least squares (3SLS). Before estimating the two-equation system, we must solve the identification problem. If each of the equations contains all the (endogenous and exogenous) variables included in the system, the model will not be identified. A necessary condition for the identification of the model is that the number of exogenous variables excluded from each equation be (at least) as large as the number of endogenous variables included (e.g., Green 1993; Wooldridge 2006; Gujarati and Porter 2010). Hence, the identification and estimation of a two-equation system requires imposing (at least) two exclusion restrictions. This raises the question of which variable(s) included in the model should be excluded from each of the equations.

To identify the “village public goods provision” and “village democracy” equations, lagged measures of the quality of village committee elections (1998-2000) and per capita village government revenue (2000) are included in the model. At the same time, the lagged election variable is excluded from the public goods provision equation, and the lagged government revenue variable is in turn excluded from the village democracy equation. It is the exclusion of each of these variables from each of the equations that will enable us to identify and estimate their parameters. The assumption underlying our identification strategy is that the quality of village elections in the previous period might have a direct impact on the quality of village democracy in the current period, but only an indirect impact on village public goods provision, through its effects on village democracy. In the same way, it is assumed that village government revenue (lagged) might have a direct effect on local public goods spending, but only an indirect effect on village democracy via local public goods provision. To the extent that these assumptions hold, both equations satisfy the order condition for identification. To further improve the model, we include an additional exogenous variable, a one-period lag of voter turnout in village committee elections (1998-2000). This variable will be used in the first-stage regression (Table 3.14) as an additional instrument for the endogenous variables and, in particular, for

the village democracy variable. It will thus not appear in the second-stage regression. Table 3.12 shows the model specification and hypotheses.

Table 3.12: Village Democracy and Village Public Goods Provision: Main Model Specification and Hypotheses

	Village public goods provision (Eq. 1)	Village democracy (Eq. 2)
<i>Measure of village democracy</i> • Village democracy index (0-5)	+	n/a
<i>Measure of village public goods provision</i> • Ln (per capita village government investment in public goods)	n/a	+
<i>Measure of intra-Party democracy</i> • Intra-Party election quality (0-1)	+	+/-
<i>Measure of bureaucratic control</i> • Policy Mandates Index (0-100%)	+/-	-
<i>Economic controls</i> • Ln (per capita village government revenue) • No. collective enterprises • No. private enterprises • No. individual businesses (<i>getihu</i>) • Ln (per capita net income) • % migrants in village labour force		
<i>Social controls</i> • Percentage of households belonging to the three largest surname groups • Inter-lineage tension index (0-1)		
<i>Demographic and geographic controls</i> • Ln (village population) • Per capita arable land (<i>mu</i>) • Percentage of flat land • Percentage of irrigated land • Ln (distance to the town, km)		
<i>Exogenous variables or instruments only included in the first-stage regression</i> • Voter turnout in village committee elections (variable lagged one period)		
<i>Exclusion restrictions</i> • Election quality index (0-5) (variable lagged one period and excluded from Eq. 1) • Ln (per capita village government revenue) (variable lagged one period and excluded from Eq. 2)		

3.5 Results and Findings

Tables 3.13 and 3.14 present the results of the 3SLS estimation of the main two-equation system. The results in Table 3.14 show that, as hypothesized, there is a two-way relationship between local democracy and local public goods provision: the two variables are positively and significantly associated with each other. In communities governed by democratically elected village committees, village heads might have incentives to allocate more spending to public goods in order to increase their chances of re-election, while villagers might have incentives to participate in village politics in order to hold village committees accountable for the provision of public goods, given that they continue to be seen as having both the responsibility and capacity to meet local public goods needs⁵⁸. Village democracy might thus affect, and be affected by, the role of village committees as public goods providers, through the channels of political accountability and participation.

Our main hypothesis – that village committee elections increase the accountability of village spending to village residents, provided that (i) elections are relatively well implemented, and (ii) village committees are granted discretionary authority over the allocation of village funds – is empirically supported. The estimated coefficient on village democracy indicates that a one-unit increase in the village democracy index is associated with a 42% increase in village spending on infrastructure (see equation 1 in Table 3.14). This implies that, by adopting a broader conceptualization of grassroots democracy – one that considers not only how village committees are elected, but also whether they have the power to govern - we can find an answer to the puzzle of why existing studies on village elections have come to such different conclusions about their effectiveness as an accountability mechanism, and to the question of why villages with better elections often fail to deliver better public goods and services. The answer (or part of it) lies in the local power structure: in most villages, village committees remain powerless.

⁵⁸ Consistent with this, Hu (2005) has found that the democratic quality of village committee elections is positively associated with the level of electoral competition and participation.

The results in Table 3.14 also show that the cadre responsibility system and intra-Party elections - have vastly different effects on village democracy and public goods provision. Our hypotheses on the impact of the cadre responsibility system are partly supported (see Tables 3.9 and 3.14). As hypothesized, the degree of control exercised by higher levels of the Party-state over village governments is negatively associated with the degree of village democracy (equation 2). At the same time, tighter bureaucratic control over village officials is not significantly associated with higher village spending on infrastructure (equation 1). These results indicate that village governments that are less autonomous from and more accountable to higher levels of the Party-state are less likely to be run by democratically elected village committees and, at the same time, are not any more likely to allocate more resources to local public goods provision. This suggests that, under the cadre responsibility system, neither are township cadres held accountable for promoting village democracy, nor are village officials held accountable for providing infrastructure. Indeed, by increasing the influence and control of township Party committees over village governance (i.e., who governs and how), the cadre responsibility system may have the (unintended) effect of making village governing bodies less (democratically) accountable to villagers, and village spending less responsive to public goods needs. These findings are consistent with previous research showing that bureaucratic institutions of accountability fail to provide “positive” incentives for village officials to use available funds to improve community infrastructure (Tsai 2007b), while creating “perverse” incentives for Party cadres at various levels to resist the implementation of democratic reforms, either by interfering in village elections (Birney 2014) or by denying village committees the authority needed to govern (Sun et al. 2013).

In contrast to the cadre responsibility system, we find that the election of village Party secretaries by village Party members has a significant positive impact on village public goods investment (first equation) and, at the same time, does not have a significant negative impact on village democracy (second equation). The results thus support the hypothesis that intra-Party elections can make village Party organizations more responsive to demands for local public goods, by creating a new relationship of accountability between village Party members and Party secretaries.

On the other hand, our results do not confirm those of Sun et al. (2013), who argue that intra-Party elections have a negative impact on the development of village democracy. This discrepancy suggests that further research is needed to determine whether, and under which conditions, intra-Party democracy can complement, rather than undermine, village-level democracy.

In addition to institutional factors, economic, social and demographic factors also explain differences among villages in terms of how much they invest in infrastructure. As can be seen in Table 3.14, the control variables included in the model behave largely as expected. Like previous studies (Tsai 2007b; Wang and Yao 2007), we find that inter-village variation in government revenue does not explain variation in public goods investment across villages. This can be interpreted as evidence of the weak accountability of village governments to villagers, who have “a strong preference for spending on public infrastructure”, as research by Luo et al. (2010: 666) has shown⁵⁹.

Also consistent with previous research are the findings that out-migration is negatively related to village public goods investment (e.g., Luo et al. 2010), while economic development - as measured by the level of per capita income - is positively associated with it (Zhang et al. 2004; Luo et al. 2007; Zhang et al. 2007). This latter finding might reflect the increased reliance of village governments on (voluntary) contributions from local residents and businesses for the construction and maintenance of infrastructure, especially after the implementation of the tax-for-fee reform (Tsai 2011: 51-54). This might be particularly the case in the richer ones, where there is greater demand and availability of resources for public goods provision.

Regarding the impact of social and demographic factors, the results in Table 3.14 show that in villages with a more homogenous social structure, where a majority of the population belongs to the same clan(s), more resources are allocated to the provision of public goods. This finding supports previous studies showing that villages where a “sizeable” proportion of the population shares the same surname

⁵⁹ Eighty percent of the villagers surveyed stated that they were “dissatisfied with the current level of infrastructure” and ninety percent of them expressed a strong preference for village governments to spend more on infrastructure, including roads, drinking water, irrigation, schools and clinics (Luo et al. 2010: 666).

tend to invest more in infrastructure (Kung et al. 2009: 69-73), while villages with multiple clans or lineages tend to invest less, and are less likely to have paved roads, running water and new school buildings (Tsai 2007b: 158-164). One of the mechanisms by which ethnic heterogeneity, in general, and clan diversity, in particular, may undermine public goods provision is the inability of members of (ethnically) heterogeneous communities to hold their leaders accountable for the misallocation of public funds, whether through the use of political institutions (e.g., Keefer and Khemani 2005) or social sanctions (e.g., Tsai 2007b).

Finally, we find, like Zhang et al. (2004), that the size of the population is negatively related to the level of (per capita) public goods spending: the per capita cost of infrastructure provision declines with the number of village residents. At the same time, population size is positively related to village democracy. A possible reason is that village committee elections are more likely to be monitored by the local offices of the Ministry of Civil Affairs and are, therefore, more likely to be better implemented⁶⁰ in larger villages.

Three main conclusions can be drawn from the results presented above. First, differences among villages in their spending on infrastructure mainly reflect differences in their (formal) governing structures and processes, as well as in their levels of economic development and social capital. Second, democratic institutions – whether in villages or within Party organizations – appear to be more effective than bureaucratic institutions in increasing the accountability of village officials for building and maintaining basic infrastructure in their communities. And, last but not least, bureaucratic and democratic institutions of accountability (i.e., the cadre responsibility system and village democracy) seem to conflict with each other.

One of the most significant findings is that variation in the degree of political decentralization or democratization at the village level is positively associated with variation in the level of investment in infrastructure *made* by village-level governments. This raises the question of whether it is also associated with inter-village variation in the level of investment *received* from higher-level governments and in what way. As discussed in section 3.4.1, the distinction made by Zhang et al.

⁶⁰ In line with this interpretation, research conducted by Hu (2005) reveals that the presence of officials from the County Bureau of Civil Administration enhances participation in, and the democratic quality of, village committee elections.

(2007: 126-131) between “own investments” and “subsidized investments” in village-level infrastructure is a crucial one, given that different types of investment might be determined by different factors. While the focus of this chapter was on examining how village governance affects (and is affected by) the allocation of spending by village leaders (i.e., determinants of decentralized spending), an exploratory analysis of what determines the allocation of (capital) grants by higher-level governments to villages (i.e., determinants of centralized spending) can provide further evidence on whether, and under which conditions, local democratic reforms matter for rural public goods provision.

Following Zhang et al. (2007), we run an additional regression using as dependent variable the share of “subsidized” investment in total infrastructure investment (2003-04). The regression results are reported in Table 3.15. They suggest that, the distribution of earmarked grants among village governments is not only determined by economic or social considerations, but also by political factors: county and township governments tend to allocate a smaller share of available grant funds to villages governed by democratically elected village committees. This finding seems consistent with case study evidence of political targeting of fiscal transfers in Shaanxi and Zhejiang provinces. In their study of how county governments allocate grants to villages for infrastructure projects under the “new socialist countryside” program, Ahlers and Schubert (2009: 55) come to the conclusion that, in addition to village development indicators, “funding decisions also depend in part on the degree of “peaceful” cooperation within a village (between the village and party committees), which ensures smooth project implementation on the ground, and on the quality of communication between the cadres bureaucracies at the village, township and county levels (...).” Thus, while the transfer system may be being used as a mechanism of fiscal redistribution, it may also be being used as a mechanism of political control.

The fact that earmarked grants are allocated on an ad-hoc, discretionary basis makes them a useful instrument for targeting resources to politically favored villages, regardless of fiscal capacity or expenditure needs considerations. The political targeting of grants enables county and township Party committees to “reward” or “punish” villages on the basis of whether their village committees and villagers

acquiesce to or challenge the way power has traditionally been distributed and exercised in their jurisdictions. If this interpretation is correct, these results suggest that, not only bureaucratic institutions (i.e., the cadre responsibility system) but also fiscal institutions (i.e., the transfer system) may negatively affect the development and functioning of local democratic institutions. Paradoxically, those villages where more progress has been achieved in creating a system of checks and balances that prevents the concentration of power in institutions or individuals that are neither elected by nor accountable to all villagers are also the ones that are less likely to be fiscally supported by higher-level governments in their efforts to provide local public goods.

Table 3.13: Results of the first-stage regression (main model)

	Ln (per capita village govt. investment in public goods)	Democracy quality index
Intra-Party election quality	0.773 (2.14)**	0.239 (0.71)
Policy mandates index	-0.005 (-0.50)	-0.032 (-3.67)***
Ln (p.c. village govt. revenue in 2000)	0.293 (2.15)**	0.061 (0.47)
No. of collective enterprises (2000)	-0.002 (0.01)	-0.362 (-1.19)
No. of private enterprises (2000)	0.014 (0.45)	-0.014 (-0.47)
No. of individual businesses (getihu) (2000)	0.004 (1.09)	0.004 (1.12)
Ln (per capita net income in 2000)	0.419 (1.08)	-0.241 (-0.66)
Per capita arable land (2000)	-3.170 (-1.57)	-2.070 (-1.10)
% of migrants in village labour force (2000)	-0.020 (-2.34)**	-0.007 (-0.85)
% of households belonging to 3 largest surname groups	0.016 (2.54)***	0.011 (1.78)*
Inter-lineage tension	-1.016 (-0.83)	-2.925 (-2.54)***
Ln (village population)	-0.629 (-1.90)*	0.101 (0.33)
% of flat land	0.005 (0.98)	0.004 (0.73)
% of irrigated land	0.538 (1.02)	0.593 (1.20)
Ln (distance to the town)	0.207 (0.98)	0.051 (0.26)
Election Procedural Quality (2000)	-0.051 (-0.36)	0.452 (3.43)***
Voter turnout rate (2000)	0.799 (1.54)	1.501 (3.09)***
Constant	2.9847 (0.82)	2.097 (0.61)
Provincial dummies	Yes	Yes
R-Squared	0.46	0.39
F-test [p-value]	3.39 [0.0000]	2.54 [0.0011]
Observations	111	111

Note: Figures in parentheses are absolute values of t-statistics

* Significant at the 10% level

** Idem, 5%

*** Idem, 1%

Table 3.14: 3SLS estimates of the relationship between village democracy and village-financed investment (main model)

	Ln (per capita village govt. investment in public goods)	Village democracy index
Ln (per capita village govt. investment in public goods)		1.064 (2.85)***
Village democracy index	0.423 (2.12)**	
Intra-Party election quality	0.555 (1.74)*	-0.514 (-1.21)
Policy mandates index	0.013 (1.19)	-0.029 (-3.12)***
Ln (per capita village govt. revenue (2000))	0.109 (1.00)	
Election Procedural Quality (2000)		0.302 (2.34)**
No. of collective enterprises (2000)	0.229 (0.76)	-0.443 (-1.37)
No. of private enterprises (2000)	0.015 (0.54)	-0.030 (-0.92)
No. of individual businesses (getihu) (2000)	0.002 (0.72)	-0.001 (-0.33)
Ln (per capita net income in 2000)	0.684 (2.06)**	-0.782 (-1.66)*
Per capita arable land (2000)	-1.764 (-0.93)	0.875 (0.36)
% of migrants in village labour force (2000)	-0.016 (-2.03)**	0.012 (1.01)
% of households belonging to 3 largest surname groups	0.011 (1.87)*	-0.007 (-0.91)
Inter-lineage tension	0.415 (0.35)	-1.867 (-1.52)
Ln (village population)	-0.747 (-2.55)***	0.955 (2.28)**
% of flat land	0.003 (0.59)	-0.0004 (-0.07)
% of irrigated land (%)	0.337 (0.70)	-0.130 (-0.23)
Ln (distance to the town)	0.180 (0.96)	-0.181 (-0.79)
Constant	1.312 (0.41)	-1.322 (-0.35)
Provincial dummies	Yes	Yes
R-Squared	0.42	-0.23
F test [<i>p</i> -value]	4.33 [0.0000]	2.00 [0.0081]
Observations	111	111

Note: Figures in parentheses are absolute values of t-statistics

* Significant at the 10% level

** Idem, 5%

*** Idem, 1%

Table 3.15: 3SLS estimates of the relationship between village democracy and government-financed investment (additional model)

	Share of public goods investment financed by higher-level govt.	Village democracy index
% of public goods investment financed by higher levels		-0.025 (-1.70)*
Village democracy index	-13.897 (-2.54)***	
Intra-Party election quality	8.165 (0.92)	0.524 (1.42)
Policy mandates index	-0.671 (-2.46)**	-0.035 (-3.44)***
Ln (per capita village govt. revenue (2000))	-4.918 (-1.68)*	
Election Procedural Quality (2000)		0.293 (2.25)**
No. of collective enterprises (2000)	-19.036 (-2.20)**	-0.821 (-2.06)**
No. of private enterprises (2000)	-1.162 (-1.55)	-0.054 (-1.54)
No. of individual businesses (getihu) (2000)	-0.122 (-1.61)	-0.002 (-0.46)
Ln (per capita net income in 2000)	0.904 (0.10)	0.020 (0.05)
Per capita arable land (2000)	4.618 (0.09)	-1.264 (-0.55)
% of migrants in village labour force (2000)	-0.085 (-0.36)	-0.012 (-1.27)
% of households belonging to 3 largest surname groups	0.029 (0.18)	0.008 (1.19)
Inter-lineage tension	71.879 (2.30)**	0.122 (0.06)
Ln (village population)	15.523 (1.91)*	0.506 (1.21)
% of flat land	0.010 (0.08)	0.004 (0.62)
% of irrigated land (%)	-0.408 (-0.03)	0.266 (0.49)
Ln (distance to the town)	2.496 (0.49)	-0.037 (-0.17)
Constant	25.684 (0.27)	1.052 (0.26)
Provincial dummies	Yes	Yes
R-Squared	0.20	0.15
F test [<i>p</i> -value]	2.56 [0.0005]	2.09 [0.0057]
Observations	111	111

Note: Figures in parentheses are absolute values of t-statistics

* Significant at the 10% level

** Idem, 5%

*** Idem, 1%

3.6 Summary

Authoritarian regimes are often “reluctant decentralizers” (Landry 2008). An analysis of the distribution of resources and authority among different levels of the Party-state in China, and between Party and non-Party institutions in its rural communities, reveals a reluctance to devolve power to villages and, within villages, to democratically elected village committees. This has implications for public goods provision in rural communities.

The objective of this chapter was to examine the institutional determinants of government performance in the provision of public goods in rural communities after the implementation of the tax-for-fee reform. Two simultaneous equations models of “village democracy” and “village-financed investment”, and of “village democracy” and “government-financed investment”, were estimated using cross-sectional survey data from 115 villages. Two main conclusions can be drawn from the empirical results. The first one is that in those villages, where (i) village elections are better implemented, and where (ii) the village committee (head) plays (at least) as important a role as the Party branch (secretary) in determining the allocation of village spending, village leaders tend to invest more in infrastructure. However, at the same time, they seem to receive a smaller share of (capital) grants from higher-level governments for infrastructure projects. This suggests that to the extent that public spending decisions are made either by county and township governments (i.e., village infrastructure projects funded by higher-level governments) or by village Party branches (i.e., village infrastructure projects funded by the village), village committee elections are unlikely to have a positive impact on the provision of village infrastructure.

There are two possible reasons. The first is that, under such conditions, elections do not provide a mechanism for accountability, inasmuch as villagers cannot (threaten to) vote out of office those who are responsible for (intergovernmental or local) resource allocation decisions (e.g., county, township and village-level Party secretaries). The second is that earmarked grants might provide a mechanism for the political targeting of transfers, and that county and township governments might target more resources to less democratic villages, that is, those that are not governed by democratically elected village committees.

A second conclusion that emerges from the empirical analysis is that the Party's accountability mechanisms have different effects on village governance. The implementation of the cadre responsibility system is not significantly and positively associated with the level of village public goods provision. However, it is negatively and significantly associated with the degree of village democracy. In contrast, the holding of elections for village Party secretaries has a significant positive impact on village public goods provision and does not have a significant negative impact on village democratic institutions. Although more research is needed, this would suggest that democratic institutions within villages and within grassroots Party organizations can complement each other in providing new channels by which village residents and Party members can hold village officials accountable for their performance. In contrast, the implementation of the cadre responsibility system conflicts with the development of democracy within rural communities, suggesting that the more accountable village officials are to higher-level Party leaders, the less accountable they are to villagers.

Overall, our analysis and discussion lead to two conclusions. First, a critical determinant of the effectiveness of village committee elections as an instrument of accountability in the domain of infrastructure and service provision is whether village committees have control over fiscal resources (i.e., the power of village committees). Second, and relatedly, the potential benefits of political decentralization in terms of accountability are compromised by processes of fiscal and administrative (re-)centralization that shift power away from village committees. Our findings suggest that the problem of poor public goods provision in Chinese villages cannot be effectively addressed by (solely) increasing earmarked grants and top-down control. Indeed, by reducing the power and autonomy of village committees, the (re-)centralization of the fiscal and administrative systems leads to a reversal of political decentralization reforms, a further weakening of local democratic institutions, and a wider "accountability gap" between the rural population and the Party-state: "plus ça change, plus c'est la même chose" (Chan 2007).

Chapter 4
Social Institutions and Local Public Goods Provision

4.1 Introduction

The design and implementation of decentralization – how much power is given to local governments and whether they are directly accountable to the local population – has important implications, not only for the way in which local officials govern, as we saw in the previous chapter, but also for the way in which, and the purpose for which, citizens organize themselves (e.g., Manor 1999; Devarajan et al. 2009). The overall goal of this chapter is to examine the development of self-governing organizations and to assess their role and impact as (non-state) providers of basic goods and services in rural communities.

There is a growing body of literature concerned with the interactive relationship between state capacity and non-state service provision in developing countries. It suggests that the relationship between state and non-state providers – whether one of complementarity or substitution - reflects and affects state legitimacy and capacity (Evans 1996; Narayan 1999; Ostrom 1996; Woolcock and Narayan 2000; Robinson and White 2001; Joshi and Moore 2004; Cammet and MacLean 2011; McLoughlin 2011; Tsai 2011; Batley et al. 2012; Bodea and Lebas 2014). This question has received growing attention in the literature on decentralization in China (e.g., Liu et al. 2012; Oi et al. 2012). Recent studies indicate that it has become increasingly difficult for grassroots officials to collect taxes and fees (Liu et al. 2012: 194) and, even more, to raise voluntary contributions from villagers for the provision of infrastructure (e.g. Chen 2008, 2014, 2015; Fock and Wong 2008; Tian 2009; Göbel 2010; Boyle et al. 2014). This has been attributed to two different factors: a decline in political trust (Oi and Zhao 2007; Tsai 2007b) and an increase in the participation in community-based organizations that substitute for state institutions in the provision of basic goods and services (Liu et al. 2012). Villagers are more reluctant to pay taxes and to make voluntary contributions to (publicly-provided) public goods in communities where *trust* in the integrity and competence of grassroots officials is lower (Oi and Zhao 2007; Tsai 2007b). This finding is in line with the political economy literature on taxation, which emphasizes both the quality and legitimacy of political institutions in explaining tax compliance (Bräutigam

2008: 4-15; Fjeldstad et al. 2012: 8-12)⁶¹. At the same time, variation in the ability of grassroots governments to tax is also explained by variation in the ability of local communities to provide themselves with public goods. It has also been found that villagers are less willing to pay taxes and fees in communities where *self-governing organizations* have become a substitute for the (local) state, by raising funds and providing services independently from it (Liu et al. 2012: 202). This finding is, in turn, consistent with the empirical literature that examines the role of non-state actors as service providers in developing countries and how it affects the relationship between taxpayers and the state (DiJohn 2010; Cammet and MacLean 2011; Tsai 2011; Sacks 2012; Ali et al. 2014; Bodea and Lebas 2014)⁶². One of its key findings is that non-state provision is negatively associated with tax compliance when it substitutes for, rather than complements, state provision (Ali et al. 2014; Bodea and Lebas 2014).

Taken together, these studies suggest that the institutional factors explaining the unwillingness of Chinese rural residents to pay taxes and to make voluntary contributions to (government-provided) public goods are not different from those observed in other developing countries: whether they choose to comply with the state's demands partly depends on the relative effectiveness and trustworthiness of state and non-state institutions as service providers or, as Bird et al. (2006, 2008) put

⁶¹ This literature argues that in countries or communities where the government does not fulfill its "fiscal contract" with the citizenry (Levi 1988; Moore 2004, 2008), where the payment of taxes leads neither to better political representation nor to better service provision, citizens are less likely to comply with their tax obligations (i.e., "fiscal exchange" theory). Similarly, it argues that a government's ability to tax depends on its legitimacy in the eyes of taxpayers, that is, in their "belief or trust in the authorities, institutions and social arrangements to be appropriate, just, and work for the common good" (Ali et al. 2014: 830). The less trustworthy or legitimate a government is or is perceived to be, the less likely citizens are to comply with its tax demands (i.e., "legitimacy" theory) (Fauvelle-Aymar 1999; Tyler 2006).

⁶² In particular, much of this literature examines whether, and under which conditions, the financing and provision of services by actors other than the state (e.g., donors, non-governmental organizations, traditional leaders, community and religious groups, private companies, etc.) may reduce state legitimacy and capacity. Their findings show that the effects of non-state service provision depend on: (i) who citizens credit (blame) for the improvement (deterioration) of services in their communities (Sacks 2012); (ii) whether the funds used to provide public services are channelled through the state or directly to non-state actors (Ghani et al. 2005; Di John 2010); and, relatedly, (iii) whether non-state service provision takes the form of "co-production" or "self-provision" or, in other words, whether the relationship between state and non-state providers is one of "complementarity" or "substitution" (Cammet and MacLean 2011; Tsai 2011).

it, on the availability of the “voice” and “exit” options in the service provision arena⁶³.

This raises the question of what determines the availability of the so-called “exit” option in the first place? Under what conditions are “substitutive informal institutions” (Helmke and Levitsky 2004) likely to emerge? To what extent are they able to fill the gap in service provision created by ineffective formal institutions, and with which consequences? The primary objective of this chapter is to identify the institutional, social and economic factors underlying the development of self-governing organizations in Chinese rural communities. It also seeks to provide a preliminary assessment of the extent to which these organizations can serve as substitutes for the (local) state in the provision of basic infrastructure and of how this may affect its capacity to govern.

There is case study evidence of the development of “autonomous” organizations (Watson 2008) and “substitutive” public goods provision (Tsai 2011) in rural China. For instance, survey data collected from 100 villages in five provinces in 2008 shows that in 30 percent of them “there had been at least one public project managed by villagers themselves” in the previous five years⁶⁴ (Tsai 2011: 58). Likewise, statistical evidence shows that villages with autonomous community organizations, such as churches, tend to have lower levels of government investment in infrastructure (Kung et al. 2009) but are more likely to have paved roads and new school buildings (Tsai 2007ab), which can be interpreted as evidence of the growth of “substitutive public goods provision” (Tsai 2011) by these community groups. Case study evidence from a poor agricultural village in Hebei province (“South Bend”) supports this interpretation (Tsai 2007b: 144-146; Tsai 2011: 9-10) and

⁶³ Hirschman’s (1970) “exit, voice and loyalty” framework has been used to examine how citizens respond to dissatisfaction with the provision of public goods and services by their local or national government (e.g., Sharp 1984; Paul 1992; Dowding et al. 2000; Bird et al. 2008; Dowding and John 2008). In some of these studies the term “exit” refers to tax avoidance and evasion (e.g., Bird et al. 2008), in others to a change of service provider (e.g., Paul 1992), and yet in others to migration (e.g., Sharp 1984). We use the term here to refer to “exit” from state to non-state providers.

⁶⁴ In this study “management of public projects” was defined as “primary control of the funds invested in the public project and oversight of the day-to-day work on the project”. “Village public projects” were in turn defined as “the provision of public goods and services including village road and bridge works; construction or renovation of village school buildings or health clinics; repair or construction of infrastructure for drinking water, irrigation, drainage, electricity, and terraced fields; management of village public forests; reforestation; and the provision of village sanitation services and waste disposal” (Tsai 2011: 57-58).

shows that in this, like in other communities, “what public goods provision exists is organized by the church management committee of the village’s Catholic church, completely independently of the village government”⁶⁵ (Tsai 2011: 9-10).

To shed light on the factors behind these forms of collective action, this chapter seeks to examine whether, and in what ways, satisfaction with and trust in state institutions affects participation in self-governing organizations. Using Hirschman’s (1970) terminology, and based on the studies cited above (e.g., Bird et al. 2006, 2008; Bodea and Lebas 2014), it is plausible to hypothesize that when state institutions fail to meet citizen demands for representation and essential public services and, by extension, fail to elicit “loyalty” (i.e., trust), citizens may choose “exit” over “voice” as a response to dissatisfaction with their performance. In other words, they may turn to non-state providers for access to basic services, while disengaging from the state in various ways. In the rural Chinese context, the lack of trust in township officials, coupled with a poor provision of village public goods and a poor implementation of village elections, might provide incentives for villagers to form or participate in self-governing organizations.

However, one thing is that citizens have an incentive to engage in more autonomous forms of organization and to cooperate in the production of certain goods and services, and another is that they have the capacity to do it. Communities may be able to do what markets and states fail to do (i.e., “market failure” and “state failure” in the form of under-provision of local public goods) (e.g., Bowles and Gintis 2012) - or they may not. The ability of groups of individuals to solve the collective action problem involved in the formation of organizations and in the provision of public goods depends on factors such as group size (Olson 1971: 53-65) and heterogeneity (Baland and Platteau 1996: 284-345), the design of institutional arrangements that facilitate cooperation among group members (Ostrom 1990: 88-102), and the “stock of social capital” – that is, of “trust, norms and networks” – within communities (Putnam 1993: 163-185).

⁶⁵ Interestingly, Tsai (2011: 54) also found that in this village “noncompliance with state policies and taxation is very high and the Party secretary complains bitterly about this lack of power over villagers. The village church has far higher standing with villagers than the village government, and church authority is reinforced by the village public projects they finance and organize”.

Two crucial aspects of the community context in rural China are lineage structure (Tsai 2007ab) and out-migration processes (Lu 2015). Consequently, we also examine how lineage and migration networks constrain or enable the development of self-governing organizations. As we shall argue in section 4.3, they might crucially affect the ability of groups of individuals to organize themselves to cope with community problems, yet in ways different from those observed in other countries. Although inter-clan conflicts and out-migration flows could create obstacles to successful collective action at the village level, this may not be the case in rural China, given the prevalence of cooperative relations between village clans, and of circular migration between rural and urban areas. Our basic hypothesis is that villages with more cohesive lineage groups and with larger migration networks may provide the social conditions for the development of self-governing organizations. This hypothesis is in line with the literature on social capital, which points to the importance for rural development of what is variously called “bonding” and “bridging” social capital (e.g., Narayan 1999), or “intra-community ties” and “extra-community networks” (e.g., Woolcock 1998), that is, different types of social networks at the community level that promote “integration” within communities, while providing “linkage” to external resources.

In addition to explaining what drives the development of self-governing organizations, this chapter also intends to explore both the limitations and unintended consequences of non-state provision by self-governing organizations. To this end, it provides a preliminary assessment of their role as (non-state) providers of basic village infrastructure, in particular, roads and bridges, drinking water and irrigation systems, as well as school buildings. Likewise, it examines whether participation in these organizations increases distrust between villagers and officials.

The remainder of the chapter is structured as follows. Section 4.2 examines the presence of self-governing organizations in Chinese villages and their performance in public goods provision on the basis of survey data of 552 community organizations. Section 4.3 develops hypotheses regarding the effects of political trust, local government performance, lineage structure, and out-migration flows on participation in self-governing organizations. In section 4.4 we present the

econometric model and estimation procedure and describe the main variables used in the model. Section 4.5 presents the econometric results, and section 4.6 concludes.

4.2 Rural Social Organizations and Non-State Provision of Basic Services

“Governance in the countryside is changing, and non-state organizations are playing a bigger role” (Deng and O’Brien 2014: 188). Village temples (Dean 2003; Chau 2005; Tsai 2002, 2007ab, 2011), farmers’ cooperatives (Augustin-Jean and Xue 2012; Deng et al. 2010; World Bank 2006), old people’s associations (Hansen 2008), and water user associations (Li et al. 2004) are a few examples of the traditional and new organizations that have emerged in Chinese villages and that provide essential goods and services to their residents.

A review of the literature on their development and role indicates that rural organizations are characterized by: (i) a high degree of informality; (ii) a strong government involvement in their formation, governance, and activities; and (iii) a focus on service delivery, rather than on advocacy. Most village organizations are not formally registered with the Ministry of Civil Affairs; have a close relationship with the state; and play a more important role in providing services than in mobilizing villagers to demand more accountability or better services from state institutions⁶⁶ (Shue 1994; White et al. 1996; Tsai 2002, 2007ab, 2011; Dean 2003; Li et al. 2004; Chau 2005; Fan et al. 2006; Hansen 2008; Unger 2008; Deng et al. 2010; Tong 2010; Augustin-Jean and Xue 2012; Bislev and Thøgersen 2012)⁶⁷.

Yet, at the same time, this literature suggests that organizations differ in terms of: (i) how much autonomy they have in relation to the state (e.g., Watson 2008); and (ii) whether they provide infrastructure and services independently or in collaboration with state actors (e.g., Tsai 2011). Thus, in the analysis of non-state organizations and non-state service provision in rural China, it is important to make

⁶⁶ This contrasts with what happens in India and much of Latin America, where “the non-state sector is not a major actor in direct provision but tends to play more of an advocacy role, mobilizing communities to demand services from the state” (Robinson and White 2001: 81).

⁶⁷ There is a significant body of literature on associational life in China during the reform period (e.g., White et al. 1996; Brook and Frolic 1997; Saich 2000, 2004; Howell and Pearce 2001; Ma 2002, 2005; Howell 2004; Unger 2008; Shieh 2009; Wang and He 2010). However, relatively less attention has been paid to the study of rural associations.

two distinctions. The first one is between self-governing and government-controlled organizations (Liu et al. 2012). “Self-governing organizations” are organizations which are institutionally separate from the state and in which local government and Party officials do not participate. Specifically, they are defined as those community-based organizations that meet the following two criteria: (1) their leaders are not appointed by, and do not hold concurrent posts in, the local Party-state; and (2) they do not incorporate local officials in their activities or decision-making processes. In contrast, “government-controlled organizations” fail to meet either or both of these criteria: they have local officials among their leaders or members and are characterized by a low degree of organizational autonomy from the state.

The second distinction is between different types of non-state provision of public goods: “substitutive provision” by non-state actors and “co-production” between state and non-state actors (Tsai 2011). The main difference lies in whether non-state actors provide services in collaboration with state agencies or independently. “Co-production” refers to “the provision of public services through a regular long-term relationship between state agencies and organised groups of citizens, where both make substantial resource contributions” (Joshi and Moore 2004: 31). In contrast, “substitutive provision” by non-state actors “replaces state provision” and “takes place independently without increasing opportunities for interaction, exchange, and reciprocity between officials and citizens” (Tsai 2011: 48-49).

The fact that there is variation among villages in the autonomy that village organizations have, and in the form that non-state provision takes, raises questions that have not been addressed in previous studies: What proportion of villages have self-governing organizations? What forms do these organizations take? How many of them are involved in the provision of infrastructure, and how effective are they?

The data in Tables 4.1 through 4.4 provide some answers to these questions. Table 4.1 shows the presence of a wide variety of social organizations in the sample villages, including wedding and funeral councils, old people’s associations, Buddhist temples and Christian churches, technical associations, mutual aid groups, consumers’ associations, public security and mediation committees, and others. Of the 552 social organizations in the sample, more than 18 percent are religious

organizations; 17 percent are cultural, recreational and health associations; 14 percent are dispute mediation committees; 14 percent are public security committees; and another 14 percent are technology associations and mutual aid groups. 96 percent of the villages surveyed by CCAP (CAS) had at least one social organization⁶⁸ in 2005⁶⁹.

Table 4.1: Classification of village organizations by type of activity

Major Activity	Top two types of organizations ^a	Organizations	
		Number	%
Weddings & funerals	Wedding & funeral councils (42), Funeral councils (2)	45	8.2
Cultural, sports & health	Old people's association (60), Folk dance associations (10)	92	16.7
Social welfare and agricultural extension	Family planning associations (18), Agricultural extension centres (9)	42	7.6
Religious	Christian churches (32), Buddhist temples & associations (13)	100	18.1
Technology	Technology associations (29), Science & Technology associations (6)	63	11.4
Mutual aid	Seasonal mutual aid groups (3), small farmers' mutual aid groups (2)	13	2.4
Rights protection	Consumer complaint centres (8), consumer associations (6)	31	5.6
Mediation	Mediation committees (77)	77	14.0
Community order & security	Public security committees (63), community patrol groups (6)	76	13.8
Others	Financial management small groups (6)	13	2.4
Total		552	100

Source: CCAP Village Survey (2005)

Note:^a Numbers in parentheses are the number of organizations in the corresponding sub-category

⁶⁸ The average village had 4.8 social organizations (standard deviation 3.1) in 2004.

⁶⁹ The number of total social organizations in China is estimated to be more than 8 million (Watson 2008).

The growth of village organizations can be seen as part of “the associational revolution” that is underway in China (Wang and He 2010: 37). However, more important than the rise in the number of organizations is the increasing diversity among them in terms of how they relate to the state and what role they play in providing public goods and services.

As can be seen in Table 4.2, while the majority of village organizations in the sample (78%) were established by the state and have remained under its control, 22 percent of them are run by villagers themselves. Perhaps unsurprisingly, virtually all family planning associations, public security and mediation committees, technology associations and consumers’ associations have close ties to the state⁷⁰. In some cases, these organizations have been formed by township and village governments, either in response to directives from higher-level governments, or as a means of better meeting “the highest priority mandates” (Birney 2014) under the cadre responsibility system (e.g., implementation of the one-child policy, promotion of social stability and economic development, etc.). This is, for example, the case of farmer professional cooperatives (e.g., technical associations), family planning associations and public security and mediation committees (World Bank 2006; Deng et al. 2010; Tong 2010; Augustin-Jean and Xue 2011). In other cases, these organizations are simply village branches of “quasigovernmental organizations” that operate nationwide, such as the China Family Planning Association, the China Association for Science and Technology or the China Consumers’ Association (Wang and He 2010).

Regardless of their area of activity, what government-controlled organizations have in common is that they are formed and run in a “top-down” manner by local officials or their appointees. The fact that the state is the main driving force behind the development of rural organizations raises doubts about the extent to which they are willing and able to serve the interests of ordinary villagers. For instance, a recent report by the World Bank (2006: 19) on China’s farmer professional

⁷⁰ More surprising, perhaps, is the finding that not all democratic supervisory small groups (*jiandu xiaozu*) (“rights protection” category) and financial management small groups (*licai xiaozu*) (“others” category) are independent from those who they are supposed to monitor and to hold accountable for the management of village finances (not shown in Table 4.2) These organizations are responsible for the “democratic supervision” of the village committee and Party branch (e.g., Alpermann 2013; Levy 2007; Su and Yang 2005).

cooperatives warns against the creation of organizations “which are simply an extension of the government” and calls for the development of “farmer-owned and – controlled organizations”.

In contrast to the above described associations, self-governing organizations have a “bottom-up” character and are run by villagers. Although they take a wide variety of forms, ranging from the so-called financial management small groups to farmers’ mutual help associations, what stands out in Table 4.2 is that most of them are either religious organizations, such as Buddhist temples or Christian churches, or lineage-based organizations, such as old people’s associations and wedding and funeral councils⁷¹. Consistent with previous studies (Croll 1999; Tsai 2002, 2007ab, 2011), our survey data show that, after decades of suppression under Mao, these organizations have re-emerged in rural areas under new forms and names (e.g., old people’s associations) to perform their traditional roles as non-state providers of services⁷², which will be discussed next. If our sample villages are representative of the country’s villages, there are reasons to think that self-governing organizations are now present in a majority (55%) of them.

⁷¹ Recent studies show that there is “a strong overlap” (Svensson 2012) between lineages and some new types of organizations, in particular, “old people’s associations” and “wedding and funeral councils” (e.g., Tsai 2007b; Tong 2010; Liu et al. 2012; Svensson 2012).

⁷² Lineage and religious organizations played a crucial role in providing public goods and social welfare during the late Imperial and Republican periods (e.g., Freedman 1958; Duara 1988).

Table 4.2 Classification of village organizations by degree of autonomy

Major Activity	Top two types of organizations ^a	Organizations	
		Govt.-controlled (%)	Self-governing (%)
Weddings & funerals	Wedding & funeral councils (42), Funeral councils (2)	78	22
Cultural, sports & health	Old people's association (60), Folk dance associations (10)	80	20
Social welfare and agricultural extension	Family planning associations (18), Agricultural extension centres (9)	98	2
Religious	Christian churches (32), Buddhist temples & associations (13)	21	79
Technology	Technology associations (29), Science & Technology associations (6)	94	6
Mutual aid	Seasonal mutual aid groups (3), small farmers' mutual aid groups (2)	85	15
Rights protection	Consumer complaint centres (8), consumer associations (6)	100	0
Mediation	Mediation committees (77)	99	1
Community order & security	Public security committees (63), community patrol groups (6)	97	3
Others	Financial management small groups (6)	77	23
Total		78	22

Source: CCAP Village Survey (2005)

Note:^a Numbers in parentheses are the number of organizations in the corresponding sub-category

As important as differences in the autonomy of social organizations are differences in their service delivery role. Survey research on rural public goods provision in the post-tax-for-fee reform era indicates that 80 percent of rural households are dissatisfied with the infrastructure provided in their villages (Luo et al. 2010: 666). It also indicates that roads, drinking and irrigation water, and schools are the types of public goods to which villagers attach the highest priority (Yi et al. 2011: 120-122). It is not clear, however, to what extent village organizations can fill the gap left by the state in the provision of these local public goods.

Table 4.3 throws some light on this. It shows the degree of involvement of both government-controlled and self-governing organizations in the provision and maintenance of roads and bridges, drinking water and irrigations systems, as well as primary school buildings, between 2000 and 2005 in the sample villages. As can be seen, 19 percent of the organizations⁷³ initiated (at least) one community project involving the construction and maintenance of roads, bridges or drinking water facilities in 2000-2005, and 67 percent of them were able to implement the project(s) successfully. The percentage of village organizations involved in the construction and maintenance of irrigation infrastructure and school buildings during this period was 16 and 12 percent, respectively. In this case, also about 70 percent of the organizations were able to complete the projects undertaken.

There appear to be both differences and similarities between government-controlled organizations and self-governing organizations in the scope, nature and effectiveness of their role as non-state providers (Tables 4.3 and 4.4). First, self-governing organizations are somewhat more likely to get involved in the provision of infrastructure. Table 4.4 shows that more than 30 percent of this type of organizations reported having initiated (at least) one infrastructure project between 2000 and 2005, although there are significant regional differences.

Second, these organizations seem less willing than government-controlled organizations to participate in the “co-production” of infrastructure projects with local officials, and more likely to raise funds and carry out such projects independently (not shown in the table). For instance, although the majority of community organizations work together with the village committee and Party branch in the design and implementation of community infrastructure projects, 50 per cent of the local temples that initiated and successfully completed (at least) one infrastructure project in the 2000-2005 period acknowledged not having sought approval or support from the two village committees to carry them out. The fact that self-governing organizations are more likely to engage in what is called “substitutive public goods provision” (Tsai 2011) may explain the finding of a recent study that

⁷³ The finding that very different types of social organizations are involved in local public goods provision is in line with the findings of recent studies showing that village-level associations are engaged in multiple activities and perform a wide variety of functions (e.g., Tong 2010).

variation in “tax resistance” or in the ability of grassroots governments to raise revenue from rural residents is associated with differences in the level of participation in self-governing organizations across villages: the higher the participation in these organizations, the lower the extractive capacity of grassroots governments (Liu et al. 2012).

Last, although government-controlled and self-governing organizations provide villagers with a means to participate in the provision and maintenance of community infrastructure, the capacity of these organizations to meet local infrastructure needs is limited, as reflected by the fact that (on average) 30 percent of those which aimed to address popular demands for better roads, drinking and irrigation water infrastructure, and school facilities were unable to do so (Table 4.3). This capacity problem seems to be more serious among certain types of self-governing organizations, such as churches (Table 4.3), and in certain provinces, such as Shaanxi⁷⁴ (Table 4.4).

In sum, the analysis of the nature and role of self-governing organizations reveals to a large extent the resurgence of clan- and religion-based organizations as non-state service providers in rural China. While in some communities these organizations are able to raise funds and provide infrastructure independently from the state, in others they are not. It would thus be unwise to overstate their ability to replace state institutions in providing rural infrastructure without considering their capacity constraints, especially in poorer areas, where investment in infrastructure is most needed. At best, they can only partly fill the infrastructure gap left by the state.

⁷⁴ Not even one percent of self-governing organizations in the villages of Shaanxi province were involved in the development of infrastructure projects in the 2000-2005 period (Table 4.4). The fact that these villages have the lowest per capita income in the sample might be one of the reasons why self-governing organizations, which depend on voluntary contributions and donations from their members, do not play a more active role in providing village infrastructure.

Table 4.3: The role of village organizations in public goods provision, 2000-2005 (%)

<i>Major area of activity or type of social organization</i>	<i>Roads, bridges, drinking water</i>		<i>Irrigation</i>		<i>Schools</i>	
	% initiating a public project	% completing the project successfully	% initiating a public project	% completing the project successfully	% initiating a public project	% of completing the project successfully
Weddings & funerals	19	86	14	80	14	80
Cultural, sports & health	35	57	21	69	17	62
Social Welfare and Agricultural Extension	19	50	23	57	17	80
Local temples	11	80	10	25	5	0
Churches & other religious organizations	12	20	7	33	2	100
Technology	15	75	20	70	8	100
Mutual aid	17	50	25	67	8	100
Rights protection	19	80	31	75	23	100
Mediation	18	85	12	78	12	89
Community order & security	11	71	11	43	6	75
Others	30	100	30	100	40	75
Total	19	67	16	65	12	78

Source: CCAP Village Survey (2005)

Table 4.4: Self-Governing organizations and public goods provision (2000-05)

<i>Province</i>	<i>Self-governing Organizations</i>	
	% involved in infrastructure provision	% not involved in infrastructure provision
Jiangsu	20	80
Sichuan	29	71
Shaanxi	0	100
Jilin	33	67
Hebei	25	75
Fujian	47	53
Total Sample	32	68

Source: CCAP Village Survey (2005)

There is a growing body of literature on the impact of lineage and religious institutions on governance and public goods provision in Chinese villages that is directly relevant to our research (Tsai 2002; 2007ab; 2011; Hansen 2008; Kung et al. 2009; Thogersen 2009). Explicitly or implicitly, much of this literature applies Peter Evans' work (1996) on "state-society synergy" to the rural Chinese context, highlighting the "complementarity" between social and state institutions, and the social "embeddedness" of state actors as a "catalyst for development" in rural China.

Of particular importance is the work of Tsai (2007ab), which draws attention to the ways in which, and the conditions under which, the presence of traditional social organizations, such as lineages and temples, allows villagers to overcome "the accountability problem" associated with *governmental* public goods provision in rural communities. She proposes a "model of informal accountability" (Tsai 2007a: 356-357; Tsai 2007b: 86-119), which posits that "in political systems with weak formal institutions of accountability, localities with encompassing and embedding solidary groups are likely to have better governmental provision of public goods than localities without these groups, all other things being equal"⁷⁵ (Tsai 2007b: 120).

⁷⁵ Solidary groups are defined as "collections of individuals engaged in mutually oriented activities who share a set of ethical standards and moral obligations" (Tsai 2007a: 356; Tsai 2007b: 4). Examples include temples, churches and lineages. These groups are "encompassing" when they are

Based on a sample of more than 300 villages from Shanxi, Hebei, Jiangxi and Fujian, her research finds that villages with temple and lineage groups, which are open to everyone in the village and which incorporate officials as members, are more likely to have higher levels of (village) government investment in public goods, and better infrastructure. She argues that “encompassing and embedding solidary groups” can improve village public goods provision by increasing “mutual accountability between villagers and officials” (Tsai 2007b: 166) – presumably, in ways that political institutions do not or cannot. In communities with these groups, officials are more likely to feel a strong social obligation to meet villagers’ demands for public goods, which in turn makes villagers more likely to be willing to comply with state policies (e.g., taxation) and to participate in the co-production of public goods with officials.

Our study differs from and complements this line of research in four ways. The first difference has to do with the type of organizations studied. Two distinctions can be made between what we call “self-governing organizations” and what Tsai (2007ab) calls “encompassing and embedding solidary groups”. First, although a majority of self-governing organizations are, or have their origins in, “solidary groups”, they do not incorporate officials as leaders or members. In other words, they may be “encompassing”, but not “embedding”. Second, our analysis of village organizations is not confined to “solidary groups”, such as religious or clan-based organizations. As we saw, self-governing organizations take a wider variety of forms, such as farmers’ mutual aid groups or cooperatives, to name a few (Table 4.1). In short, the focus of our analysis is on voluntary community organizations, which may or may not be based on “solidary groups”, but which are not intertwined with the state.

The second difference is related to the forms of public goods provision that are the focus of the analysis. As previously discussed, the presence of “encompassing and embedding solidary groups” is positively associated with higher levels of “state provision” by village governments (Tsai 2007ab) and of “non-state provision” in the form of “coproduction” between village governments and community groups (Tsai

“open to everyone under the local government’s jurisdiction”, and “embedding” when they “incorporate local officials into the groups as members” (Tsai 2007a: 356, Tsai 2007b: 13).

2011). By enabling villagers to use social sanctions against corrupt or incompetent cadres, these groups help address “the accountability problem” that prevents cooperation between village officials and villagers in the context of public goods provision (Tsai 2007ab). Unlike these organizations, self-governing organizations lack leverage over officials and, consequently, may be less able to hold them accountable for providing public goods⁷⁶. They may also be less willing to engage in the co-production of public goods with local officials. However, as previously discussed, some of them are able to and do provide public goods themselves. These organizations may thus help villagers overcome the “collective action problem” associated with what is called “substitutive nonstate provision” (Tsai 2011). The literature on social capital suggests that membership in these organizations might reduce the free-riding problem associated with the (voluntary) provision of public goods in (at least) three ways: (i) by fostering “norms of reciprocity” among community members; (ii) by generating “information” about the behaviour of individual members; (iii) and by increasing the credibility of “social sanctions” against opportunistic or untrustworthy behaviour (Putnam 1993: 174). In all these ways, the presence of self-governing organizations may create the conditions for villagers to cooperate and to provide themselves with basic public goods that are under-provided by the state.

A third difference between our study and the work of Tsai (2002, 2007ab, 2011) has to do with the direction of the causal relationship between social organizations and institutional performance. Reflecting the influence of Putnam’s work, the main aim and contribution of her research is to explain how certain forms of social organization may (positively) affect local government performance. In this chapter, we examine the interactive relationship between both variables but, in line with research by Rothstein (Rothstein and Stolle 2008) and other scholars (Tendler 1997; Ostrom and Ahn 2001), we emphasize the opposite direction of their causal relationship, that is, the impact of (local) government performance on villagers’

⁷⁶ The only way in which these organizations could hold local officials accountable is by engaging in confrontational forms of collective action, but this is not the focus of the present chapter. Recent research by Hurst et al. (2014) suggests that the presence of what they call “semi-autonomous organizations with mediating capacity”, such as old people’s associations, helps contain large-scale petitions and protests against local officials.

initiative to form or join self-governing organizations. This is because there are grounds to believe that “national, regional, and local governmental institutions strongly affect the level and type of social capital available to individuals to pursue long-term development efforts” (Ostrom and Ahn 2001: 16). Last, unlike in Tsai’s model of informal accountability, the main causal mechanism linking rural social organizations and local government performance in our research is not social control, but instead political trust. We examine whether political trust is shaped by, and shapes, the performance of state institutions, through villagers’ participation in self-governing organizations.

Finally, to illustrate the similarities and differences between self-governing and government-controlled organizations, Boxes 4.1 and 4.2 provide an example of each type of organization: the village elders’ association in Liyuan village (Liu et al. 2012) and West Gate village (Tsai 2007b). Both organizations are old people’s associations; both have their origins in lineage or clan groups; both are located in Fujian province; and both contribute to improving access to basic infrastructure in their communities. However, they differ in the way they relate to the state, and in the strategies they adopt to improve the provision of infrastructure in their villages. The association in Liyuan is an example of a “self-governing organization” (Box 4.1), while that in West Gate exemplifies what we call “government-controlled organizations” (Box 4.2). In the next section (4.3), we develop hypotheses regarding the determinants of participation in self-governing organizations on the basis of the existing literature.

Box 4.1: The Village Elders' Association of Liyuan (Fujian)

“The Village Elders’ Association was established in 1985 by a villager working in Fuzhou as a construction worker, Chen Wangti. Starting in 1996, however, VEA got more actively involved in managing village affairs, such as building a theatre, temple, road (...). In 2004, VEA initiated a project of building a cement road and mobilized its members for funding. Before long, it collected more than 500,000 yuan in contributions, an amount larger than the actual cost of the project. VEA’s effective resource mobilization derived from the prestige it enjoyed among the villagers. In terms of organizational building, the VEA governing body consisted of seven members. Each of the seven families (Lin and Huang being the two largest families) in the village recommended one elder from their families and ran the daily operations of the VEA. These highly respected elders have won VEA the trust among village residents. Their credibility was further enhanced by its handling of financial affairs. Because of the implicit checks and balances in its governance, VEA handled all financial matters in a relatively open fashion. Villagers knew how their money was spent therefore were willing to contribute to the cause. Finally, through relatives living in the village, VEA reached fellow family members thousands of miles away in the cities or abroad and solicited their financial contributions. Interestingly, VEA, being non-governmental, had actually broader mobilization network than village committees and party organizations” (Liu et al. 2012: 195).

Box 4.2: The Village Elders' Association of West Gate (Fujian)

“West Gate has a temple community council that plays a significant role in village affairs and governance (...). Village officials are deeply embedded in the temple’s institutions and activities. Both village officials and council members see their interests as complementary, so much that in 1996, when the district government directed all its villages to set up senior citizens’ associations, village officials and council members agreed to make the temple council (which had already been operating since the 1980s) the village senior citizen’s association. By giving the council this official title the council head explained, village officials would be able to attend and participate in the council’s activities, which before they had avoided in accordance with the state’s ban on ‘feudal superstition’, and the council would be camouflaged from state censure (...). The temple council exerts a significant amount of leverage over village officials. Council members report that they regularly seek out the village Party secretary and village head ‘to tell them the good and bad things they are doing’. In comparison to neighboring villages (without villagewide temple groups), West Gate’s officials organize an impressive array of public services, ranging from dumpsters and sanitation works, to paved village roads bordered with rudimentary gutters. According to West Gate’s villagers, the village’s temple groups take the lead in collecting donations to repair a local road or build a drainage system and then push the village government to fund the rest of the project” (Tsai 2007b: 139-141).

4.3 Hypotheses Development

4.3.1 Political Trust

A rational view of “trust” sustains that it is based on assessments of the trustworthiness of the potentially trusted person or institution (Hardin 2006; Levi 1998; Levi and Stoker 2000). “Individual trustworthiness” implies both “commitment to act in the interests of the truster” and “competence in the domain over which trust is given” (Levi and Stoker 2000: 476). “Institutional trustworthiness” involves “procedures for selecting and constraining the agents of institutions so that they are competent, credible, and likely to act in the interests of those being asked to trust the institution” (Levi 1998: 80)⁷⁷.

In most decentralized countries, trust in government varies across levels of government, however countries differ in how much trust citizens have in their central and local governments (Pharr 1997; Jennings 1998; Levi and Stoker 2000; Denters 2002; Kincaid and Cole 2010; Tang and Huhe 2014). In the United States (Jennings 1998), much of Western Europe (Denters 2002) and Japan (Pharr 1997), local governments are considered more trustworthy than the central government. This also appears to be the case in most sub-Saharan countries (Bratton 2012). In contrast, in some East Asian and Latin American countries, such as China, Mexico, or Vietnam, the opposite is true: citizens trust the central government, but do not trust local governments (Li 2004; Kincaid and Cole 2010; Tang and Huhe 2014).

There is a growing body of literature on political trust in rural China and its effects on tax compliance and on political and social participation (O’Brien and Li 1995; Shi 2001; Li 2004, 2008, 2011; Manion 2006; Saich 2007, 2008; Tao et al. 2011; Liu et al. 2012). These studies show that, like their urban counterparts, rural residents “do not experience the Chinese state as a single entity with a single face” (O’Brien and Li 1995: 782), and that they “disaggregate” the state into “trustworthy higher levels” and “untrustworthy lower levels” (Li 2004: 231-232).

⁷⁷ The first paragraph of this section draws heavily on Pesqué-Cela et al. (2009: 156-157).

This literature also suggests that the growing lack of trust in rural governments manifests itself in five ways. One is a decline in tax compliance. Since the rural tax reform was implemented, “tax resistance” has not so much declined as changed in form. Years ago, farmers resisted the “arbitrary” imposition of taxes and fees by local officials mainly through “violent” protest (Bernstein and Lü 2000, 2003, 2008). Today, they resist paying “perfectly legal” taxes and fees in a “passive” way (Liu et al. 2012: 194). This is especially the case in communities where villager-cadre relations have deteriorated, “with peasants often expressing ill feelings toward township and village cadres” (Oi and Zhao 2007: 87).

Another sign of the declining legitimacy of grassroots governments is their inability to raise voluntary contributions from villagers for infrastructure projects under the so-called “one-issue-one-discussion” (“yi shi yi yi”) system, a new form of “participatory budgeting” promoted by the central government (e.g. Chen 2008, 2014, 2015; Fock and Wong 2008; Li 2009; Tian 2009; Göbel 2010; Boyle et al. 2014). In communities where confidence in village officials has been undermined by problems of corruption, villagers refuse to pay 15-20 yuan annually to build and repair basic infrastructure, such as roads and irrigation systems (Chen 2008, 2014, 2015). “Yi shi yi yi is really good”, they say, “village cadres do not work and we do not waste money” (Chen 2008: 332).

A third consequence of the growing cleavage between villagers and local officials is the decline in voting and other forms of “institutionalized” political participation. In villages where distrust of township officials is high, and where neither elections nor village assembly meetings provide opportunities for meaningful participation in village governance, villagers disengage from the political arena (Tao et al. 2011). They point to their “lack of political influence” as the main reason for their lack of interest and participation in village politics (Schubert and Ahlers 2012a: 100), while complaining that elections are just for “show” (Tsai 2002: 15; Hu 2008: 616; Tao et al. 2011: 109) and that village assembly meetings are “tedious and futile” (Schubert and Ahlers 2012a: 152).

Distrust of local officials is also reflected in the reluctance of villagers to join economic and social organizations that are actively promoted by them. This, for instance, explains the limited success of government efforts to increase participation

in farmers' professional cooperatives (Shen et al. 2005; World Bank 2006; Deng et al. 2010). The fact that most of these organizations are established and run by local cadres raises "suspicion" among villagers, who see them as "tools" in the hands of local governments and large agribusiness firms (Augustin-Jean and Xue 2012: 196-197). Small farmers wonder whether they are being created to help them access credit and technology, cheaper inputs and new marketing channels, or whether instead "the local authorities just want to charge fees or something like that from our pocket" (Augustin-Jean and Xue 2012: 192; 196).

The fifth major consequence of the tension between villagers and rural officials is an increase in less or "non-institutionalized" forms of political participation, ranging from peaceful petitioning to violent protest. The combination of trust in the central government and distrust of local officials leads villagers to engage in what is called "rightful resistance" (Li and O'Brien 1996; O'Brien 1996; O'Brien and Li 2006) - a form of popular contention that entails the innovative use of the regime's policies and laws in order to resist local officials who deny villagers the rights granted to them by the central government (O'Brien and Li 2006: 2). Through the letters and visits system, villagers lodge complaints against "arbitrary and self-serving" rural officials at higher levels of government, often to demand that they "work hard and live plainly and be willing to serve the people" (O'Brien and Li 2006: 54; 9).

When not satisfied with the process and outcomes of petitioning, villagers resort to violent collective action (Li L. 2008). Abuses of power and public trust by township and village governments explain the sharp increase in the number of violent protests in rural areas, most of which have been organized against officials who misappropriate public funds, impose illegal taxes, expropriate land without (or with little) compensation, manipulate village elections, or turn a blind eye to the environmental and health problems caused by enterprises in their jurisdiction (Bernstein and Lü 2000; 2003, 2008; Guo, 2001; Jing 2003; Zweig 2003; Thornton, 2004; Deng and O'Brien 2014). In sum, an analysis of the literature reveals an unprecedented deterioration of state-society relations in China's rural areas since 1978.

These studies show how villagers' perceptions of the trustworthiness of rural officials shape their behaviour in the tax, political and social arenas. In so doing, they tend to portray villagers either as "alienated apathetics" (Seligson 1980), who disengage from the public sphere, or as "alienated activists" (Seligson 1980), who engage in violent collective action. However, the repertoire of societal responses to the decline of legitimacy of the local state may be wider. In this sense, the development of self-governing organizations and the growth of (substitutive) non-state provision may be other symptoms or manifestations of the lack of public trust in the willingness and ability of grassroots governments to meet local needs.

This lack of trust may reduce the incentives of villagers to cooperate with officials, while strengthening their incentives to cooperate among themselves in order to address community needs. It may lead them to form and participate in village organizations that are autonomous from the state and that are able to raise funds and provide services independently from it. Based on this discussion, it is hypothesized that lower levels of trust in grassroots officials may be associated with higher levels of participation in self-governing organizations.

To test this hypothesis, we examine villagers' assessments of the trustworthiness of township officials. This is for two reasons. First, the analytical focus is on political actors, rather than on political institutions, because research on political trust suggests that, in explaining participatory behaviour, "distrust of government may not be as important as distrust of particular authorities" (Levi and Stoker 2000: 495). Second, the focus is on township officials, rather than on village officials, because, as we saw in chapter three, they crucially influence how and by whom villages are governed but are not themselves subject to elections or any other form of control by villagers. It is this interference of the township in village governance that may explain why villagers choose to participate in self-governing organizations.

4.3.2 Local Government Performance

Institutional and cultural theories of political trust offer different views of the relationship between political trust and government performance (Newton and Norris 2000; Mishler and Rose 2001; Shi 2001; Wong and Hsiao 2011). Cultural theories argue that the origins of political trust lie in the cultural values and norms that are acquired through socialization. From a cultural perspective, political trust is “an extension of interpersonal trust, learned early in life and, much later, projected onto political institutions, thereby conditioning institutional performance capabilities” (Mishler and Rose 2001: 31). In contrast, institutional theories contend that political trust is a rational response on the part of individuals to the performance of government institutions and leaders. It is not a cause but a consequence of institutional performance (Mishler and Rose 2001: 31).

The results of cross-country studies testing these competing theories in the United States, Western Europe, Eastern and Central Europe, the former Soviet Union, as well as East Asia (including China), support the superiority of institutional explanations of political trust (Newton and Norris 2000; Mishler and Rose 2001; Wong and Hsiao 2011). However, the ongoing debate on whether political trust is politically exogenous or endogenous and on the relationship between political trust and government performance has significant implications for our research⁷⁸: it suggests that it might be necessary to examine the impact of objective measures (rather than subjective perceptions) of local government performance on villager participation in self-governing organizations. Doing so will allow us to determine: (a) whether the performance of government institutions has a direct impact on participation in self-governing organizations or an indirect impact through political (dis-)trust formation; and (b) which dimensions of local government performance, if any, are most important in shaping villagers’ beliefs about the trustworthiness of their leaders.

⁷⁸ More specifically, it raises the question of whether political trust can be considered a good proxy for government performance (as largely assumed in the previous section).

In China, the aspects of local government performance that matter most to villagers are: the provision of local public goods and the implementation of village democratic reforms⁷⁹. Our basic hypothesis is that, all else being equal, a poorer provision of public goods and a poorer implementation of village elections (a) may directly increase participation in self-governing organizations; and (b) may indirectly increase participation rates, by reducing political trust in grassroots officials.

First, there might be a direct link between the performance of grassroots governments and the development of self-governing organizations. When local governments fail to meet villagers' demands for representation and for service provision, they may choose to participate in self-governing organizations as a response to dissatisfaction with their performance.

There is ample evidence that grassroots governments often fail to deliver what villagers demand: accountable and responsive governance.

Many villagers consider that VCs do not adequately represent villagers' interests, and that decisions are made by a small inner circle dominated by the Party branch and its secretary. Many also feel that village leaders have only very limited influence, and that both their and their villagers' wishes will not be taken into account by the township and county governments when decisions are made. Leakage of funds is also a problem, with villagers accusing township and county officials of siphoning off funds intended for village development or poverty reduction. (Plummer and Taylor 2004: 81)

There is also evidence that traditional social organization, such as temple or lineage-based organizations, are generally seen by villagers as an example for grassroots governments to follow, both in terms of how they are governed and how they respond to community needs.

The village government is corrupt (*fubai*), but the leaders of local religious associations would not dare (*bu gan*) to embezzle collective properties; the village government is broke and does nothing for collective welfare (*gongyi*), but the temple builds streets, schools and old people's homes; the village government's accounting practices are obscure, while ancestral halls and temples make theirs public. (Brandstädter and Schubert 2005: 809)

⁷⁹ Two criteria commonly used to evaluate local government performance in developing countries are responsiveness and accountability (Andrews and Shah 2003). Hence, the choice of "village election quality" and "public goods investment" as proxies for local government performance is also supported by the general literature.

This suggests that in communities where state institutions can neither provide sufficient public goods nor provide sufficient democratic accountability, self-governing organizations may emerge as a way of filling the gap in village governance.

Second, the performance of local governments may affect participation in self-governing organizations indirectly, through its effects on political (dis-)trust formation. A comparison between the survey findings of Saich (2007, 2008) and those of Li (2004) suggests that there is a relationship between the (perceived) quality of government performance across various indicators, including service provision, and the level of trust in various levels of government. Specifically, their findings show high levels of satisfaction with, and trust in, the central government that decline dramatically with each level of local government. In Saich's (2007, 2008) study, 86 percent of respondents (n=3,697) reported being "very satisfied" or "somewhat satisfied" with the performance of the central government, but this percentage dropped to 75 percent for the provincial level, to 52 percent for the district and county levels, and to around 44 percent for the township, village and urban street levels. Similarly, the study of Li (2004) found that 53 percent and 42 percent (n=1,259) of respondents believed that the central government and provincial governments enjoyed "a very high level of trust", but this percentage was 26%, 16%, and 13% for county-, township- and village-level governments, respectively⁸⁰.

Perceptions about the trustworthiness of government might not only be influenced by the quality of public services, but also by the quality of village elections. Research by Manion (2006: 308) shows that variation in the degree of electoral contestation and participation across villages is associated with variation in the percentage of villagers reporting that "most local leaders are clean and not corrupt". Her research suggests that, the more competitive village elections are, the more trustworthy local officials are perceived to be. To conclude, whether directly or indirectly (via political trust), the quality of local government may affect participation rates in self-governing organizations: specifically, it is hypothesized that the poorer the performance of local governments, in terms of processes (i.e.,

⁸⁰ China differs from most decentralized countries in that the level of dissatisfaction with and distrust of government increases "as government gets closer to the people" (Saich 2007: 5).

village election quality) and outcomes (i.e., public goods investment), the higher the participation in self-governing organizations is likely to be.

4.3.3 Lineage Ties

A crucial aspect of the community context in rural China is lineage structure⁸¹. Much of the empirical literature from both developed (e.g., Alesina et al. 1999; Alesina and La Ferrara 2000) and developing countries (e.g., Okten and Osili 2004; Miguel and Gugerty 2005) indicates that ethnic heterogeneity is associated with: (i) lower levels of participation in community activities (Alesina and La Ferrara 2000); lower levels of (monetary and time) contributions to community organizations (Okten and Osili 2004); and lower levels of public goods provision (Miguel and Gugerty 2005).

These findings are attributed to four main factors, some of which are interrelated. *First*, people living in ethnically fragmented communities are less likely to participate in community activities, particularly in the presence of “mixed groups”, given that “individuals prefer to interact with others who are similar to themselves in terms of income, race or ethnicity” (Alesina and La Ferrara 2000: 850). *Second*, members of different ethnic groups generally have different preferences for public goods and, consequently, are both less likely to agree about which public goods should be provided in the community (Alesina et al. 1999), and less willing to contribute to the provision of “compromise types” (Miguel and Gugerty 2005). *Third*, individuals living in heterogeneous communities may derive different utility from the welfare of different community members, depending on whether they are fellow (ethnic) group members (positive utility) or not (no or negative utility). As a result, they may be less willing to pay for goods and services that are not enjoyed

⁸¹ Like castes, tribes and other ethnic groups, lineages identify and organize themselves around claims of common descent (Tsai 2007b: 149). In the pre-revolutionary period, lineage organizations, together with religious institutions, constituted “the most important organizational reality” in rural China (Brandstädter 2003: 90). However, this changed dramatically with the establishment of the People’s Republic of China in 1949. Under Mao, the state sought to eliminate lineage organizations, as clan identity threatened to dilute class consciousness among Chinese peasants (Perry 1985: 15-16). With the introduction of economic reforms in the post-Mao period, lineages have re-emerged in rural areas, particularly in the Southeastern provinces, where lineage genealogies have been compiled, ancestral halls rebuilt, and rituals resumed (e.g., Liu and Murphy 2006; Hansen 2008; Svensson 2012).

exclusively by members of their group (Alesina et al. 1999; Vigdor 2004; Habyarimana et al. 2007). *Fourth*, social sanctions against free riders are weaker in ethnically heterogeneous communities (Miguel and Gugerty 2005; Habyarimana et al. 2007). The reason given is that social sanctions are “strong” within groups and “non-existent” across groups (Miguel and Gugerty 2005: 2331), due to “the dense networks of information and mutual reciprocity that exist in groups but that are not possible across groups” (Miguel and Gugerty 2005: 2330).

This body of literature suggests that ethnic diversity may have a negative impact on local governance in (at least) two ways: (i) it may weaken the incentives of individuals to form or join organizations (i.e., “taste for homogeneity”) and to contribute to public goods from which non-co-ethnics cannot be excluded (i.e., “taste for discrimination”); and (ii) it may increase the transaction costs of collective action, by making decision-making more difficult (i.e., diversity of preferences over public goods) and/or by making free-riding easier (i.e., weakness of social sanctions).

However, their findings might not fully reflect the way in which, and the channels through which, clan diversity affects local governance in China. Recent research has found no evidence that in villages with multiple lineages “different lineage groups prefer different types of public goods, prefer not to fund public goods that benefit people in other groups, or trust each other less” (Tsai 2007b: 167). In fact, there is evidence that villagers in single-lineage villages and in multi-lineage villages differ neither in their willingness to make voluntary (monetary and labour) contributions to public goods, nor in their ability to overcome the free-rider problem and to engage in collective action (Tsai 2007b: 166-169). Two conclusions can be drawn from these findings. First, in rural China lineage diversity does not equate with a lack of social cohesion: inter-lineage relations in multi-lineage villages are not inherently conflictual. Second, and relatedly, the fact that the level of trust and cooperation among villagers in multi-lineage villages is not lower than in single-lineage villages can be interpreted as evidence of: (i) the existence of “networks of information and mutual reciprocity” (Miguel and Gugerty 2005: 2330), not only within groups, but also across groups; and consequently of (ii) the ability of multi-lineage villages to impose social sanctions on opportunistic behaviour, and to do it effectively.

This discussion suggests that villages with multiple lineage groups, which represent the overwhelming majority of our sample villages, might not have lower levels of associational activities or (voluntary) provision of public goods. We would not expect lineage diversity, per se, to be negatively associated with the development of self-governing organizations, unless intra-lineage cohesion is gained at the expense of inter-lineage conflict, which may happen in a small number of villages. Furthermore, while the presence of multiple clans might not weaken a community's capacity for collective action, our finding (chapter 3) and those of other studies (Tsai 2007ab; Kung et al. 2009) that multi-lineage villages tend to have lower levels of (village) government investment in public goods suggests that it is precisely in these communities where incentives for self-organization and self-provision might be strongest.

In light of these considerations, in our analysis of the determinants of participation in self-governing organizations we examine the effects of both a community's lineage structure and relations and anticipate that, in the absence of inter-lineage conflict, the co-existence of active lineage groups in a village might be positively associated with participation in this type of organizations. This hypothesis is in line with recent evidence from developing countries showing a positive relationship between ethnic heterogeneity and the private provision of public goods (Kimenyi 2006; Schündeln 2013).

4.3.4 Labour Migration

Another contextual variable that might crucially affect associational life and non-state service provision in rural communities is out-migration. During the reform period, China has been experiencing what is considered “the largest migration in human history” (Roberts 2002: 141): the number of rural-urban migrants increased from less than 16 million in the 1980s to more than 158 million in 2011 (Hu et al. 2011: 64; Lu 2015: 11).

Much has been written on the socioeconomic effects of rural-urban migration on rural communities (e.g., Murphy 2002, 2009), but less attention has been paid to its sociopolitical effects. Evidence from the United States and other developed

countries indicates that (internal) migration has a negative impact on civic engagement and social capital (Putnam 2000: 205). However, migration in China, like in many other developing countries, is predominantly circular: “migrants regularly return to their villages and retain their ties to the land as part of a strategy of spatial and sectoral diversification of household labor” (Roberts 1997: 250)⁸². Circular migration does not necessarily break traditional ties within rural communities (Brown 2002; Hare 1999) and at the same time it creates new ties to urban communities, which provide (non-migrant) villagers with access to resources otherwise unavailable. Supporting this view, Matthews and Nee (2000: 613) point out that “custom requires male migrants to maintain their social ties and status in the village community by sending regular remittances to support their families. Otherwise they risk losing face not only among relatives and neighbours in the village, but also within the emigrant network of fellow villagers in the city”.

Seen in this light, one reason why rural-urban migration may be positively associated with the development of self-governing organizations in rural areas is related to the resources embedded in migration networks - the “sets of interpersonal ties that link migrants, former migrants, and nonmigrants in origin and destination areas by ties of kinship, friendship, and shared community of origin” (Massey 1990: 7). Through their (economic and social) remittances (e.g., money, skills, information, etc.), migrants can and do provide crucial support to their families and home communities in various ways (Murphy 2002, 2009). In particular, (return) migrants can contribute to the growth of non-state provision of public goods in their villages, either by making donations to community infrastructure projects (Liu et al. 2012) or by providing leadership to the community organizations that carry them out (Ge et al. 2011).

Another reason why higher levels of out-migration might result in higher levels of participation in self-governing organizations in rural areas is related not to the resources that migration brings, but to the needs that it creates. As a consequence of migration, new social organizations have emerged both in urban and rural areas

⁸² Permanent migration to cities is often neither feasible nor desirable, due to the restrictions imposed by the household registration system (*hukou*), as well as to the harsh working and living conditions faced by rural migrant workers (Davin 1998; Solinger 1999; Wang 2005; Chan and Buckingham 2008).

that help migrants and non-migrants cope with the difficulties they face (Howell 2009; Tong 2010; Watson 2008)⁸³.

In the city, rural migrant workers (*mingong*) have responded to being denied their labour rights and access to basic services by forming advocacy and service delivery organizations, such as labour non-governmental organizations⁸⁴ (Watson 2008; Zhang and Smith 2009) and schools for their children (Howell 2009). In the village, new social organizations have been formed to offset the negative impact of migration on the welfare of those “left-behind” (i.e., women, children and the elderly), such as womens’ organizations and old people’s associations (Tong 2010). These organizations can help women cope with farm work, in addition to child and elder care (Biao 2007; Mu and van de Walle 2011). They may play an important role in meeting the needs of (non-migrant) villagers and in performing the social welfare functions (e.g., elderly care) that the state is unwilling or unable to perform. For these reasons, (circular) rural-urban migration may be positively associated with the development of self-governing organizations in rural communities.

⁸³ The literature on social capital and collective action suggests that village-based migration networks, like other types of social networks, may create incentives for villagers – whether living in the village or not – to cooperate and to contribute to the community, by providing a mechanism for monitoring and sanctioning behaviour that deviates from community norms and expectations (Ostrom and Ahn 2001).

⁸⁴ Most of these organizations tend to assume a service delivery role rather than an advocacy role. They provide crucial services to migrant workers, including legal advice and support, education on labour laws and regulations, and training on occupational health and safety. Most of them are funded by international donors (Zhang and Smith 2009).

4.4 Variables, Econometric Model and Estimation Method

The central question addressed in this chapter is: what determines participation in self-governing organizations in rural communities? As discussed in section 4.2, we define self-governing organizations as those community-based organizations meeting the following criteria: (1) their leaders are not appointed by, and do not hold concurrent posts in, the local Party-state; and (2) they do not incorporate local officials in their activities or decision-making processes.

We test the hypotheses put forward in section 4.3 by estimating a two-equation model, in which “political trust” and “participation in self-governing organizations” are the jointly dependent variables. The advantage of using a simultaneous equations model is that it takes into account the possible endogeneity of the political trust variable. Political trust may both affect and be affected by participation in self-governing organizations. This possibility is suggested by the recent finding that village cadres believe that “substitutive public goods provision” by community groups undermines their authority and has a negative impact on cadre-villager relations (Tsai 2011).

The two-equation model is estimated using the three-stage least squares (3SLS) method. As discussed in section 3.4, the main reason why we use three-stage least squares, rather than two-stage least squares, is that system estimation methods are considered more efficient than single-equation estimation methods (Wooldridge 2006: 567). The remainder of the section discusses the variables included in the model and their measurement, as well as the identification strategy used to estimate the model by 3SLS.

4.4.1 Political Trust and Participation in Self-Governing Organizations

The first dependent variable in the model is the participation rate in self-governing organizations at the village level in 2004-2005. It is calculated by dividing the total number of memberships in self-governing organizations by the total village population during this period.

Table 4.5 shows the rates of participation in self-governing and government-controlled organizations in the sample villages (2004-2005). As can be seen, self-governing organizations accounted for around one-third of memberships in all organizations. Participation rates in self-governing organizations ranged from 0 to 81 percent, with an average participation rate of 4 percent. There is evidence of significant variation in the level of participation in these organizations across provinces. The average participation rate in Fujian was 15 percent as compared to only 0.2 percent in Sichuan. This indicates that villages differ not only in the “vibrancy” of their associational life (Putnam 1993) but also in the nature or character of their associations: the question is thus not – or not only – whether villagers participate in associational activities, but in which organizations they participate and why.

Table 4.5: Participation rates in self-governing organizations, by province

	No of villages	Self-governing	Government-controlled	All types of organizations
Jiangsu	19	2.08	8.38	10.46
Sichuan	20	0.21	2.75	2.96
Shaanxi	16	4.08	4.81	8.89
Jilin	21	1.65	9.81	11.46
Hebei	19	1.55	4.64	6.19
Fujian	20	15.07	17.20	32.27
Sample	115	4.13	8.08	12.21

Source: CCAP Village Survey (2005)

The second dependent variable is political trust. A village-level measure of political trust was created, using responses from villagers to five survey questions about the integrity and competence of township officials. As can be seen in Table 4.6, questions 1-2 asked respondents to assess the trustworthiness and reputation (*weixin*) of both township officials and those awarded the title of “model cadre” and “model Party member” by the township government. Questions 3-5 asked respondents to assess the willingness and ability of township officials to serve their interests and needs. A dichotomous variable was created for each of the political trust questions. Each variable was coded 1 if the respondent answered “agree” or “somewhat agree”, and 0 otherwise. We then combined the five variables into an index, by averaging them. The political trust index, ranges from 0 to 1, with higher scores indicating higher levels of political trust. Table 4.7 reports the average value of the index and its components across villages by province. A comparison of Tables 4.7 and 4.5 suggests that there might be a link between levels of political trust and patterns of social participation. Villages in Sichuan and Fujian are the ones with the highest and lowest scores on the political trust index (Table 4.7), and are also the ones with the lowest and highest participation rates in self-governing organizations (Table 4.5).

Table 4.6: Survey questions on the trustworthiness of grassroots officials

1. Do you agree that township officials are highly respected by villagers?
2. Do you agree that “model cadres” and “model Party members” are held in high regard?
3. Do you agree that township policies truly promote the interests of peasants?
4. Do you agree that township officials are willing to uphold justice for peasants?
5. Do you agree that addressing complaints to township officials is an effective way to solve problems?

Table 4.7 Political trust index scores, by province

	Township cadres respected	Model cadres highly regarded	Township policy beneficial	Willingness to uphold justice	Ability to solve problems	Political trust index
Jiangsu	0.37	0.41	0.53	0.60	0.66	0.51
Sichuan	0.46	0.47	0.65	0.76	0.86	0.64
Shaanxi	0.27	0.34	0.37	0.47	0.70	0.43
Jilin	0.43	0.54	0.52	0.62	0.65	0.55
Hebei	0.37	0.32	0.47	0.56	0.65	0.47
Fujian	0.32	0.26	0.34	0.39	0.58	0.38
All sample	0.37	0.39	0.48	0.57	0.69	0.50

Source: CCAP Village Survey (2005)

4.4.2 Local Government Performance

Two (time-lagged) measures of local government performance are included in the model: village public goods provision and election quality. The variable “village public goods provision” refers to (per capita) village government investment in infrastructure in 2003-2004. “Election quality” refers to the democratic quality of the last village election before 2004. It is measured by an election quality index, which ranges from 0 to 5, with higher scores denoting freer and fairer elections, in which: (1) election committee members were selected by villagers; (2) candidates were directly nominated by voters through open primaries (i.e., *haixuan*); (3) secret voting booths were used; (4) proxy-voting was not permitted; and (5) roving ballot boxes were not used⁸⁵.

Table 4.8 reports the average values of the government performance variables in our sample villages. During the period of study, villages in Sichuan recorded the highest level of infrastructure investment (188 yuan per capita), and villages in Hebei the lowest (66 yuan per capita). Villages in Jilin obtained the highest score in the

⁸⁵ A more detailed explanation of these variables was given in section 3.4.1. It should be noted that the measure of “village public goods provision” in this chapter only includes capital expenditures on infrastructure.

election quality index (3.29), and villages in Shaanxi the lowest (1.75). A comparison of Tables 4.7 and 4.8 suggests that there might be a link between how much local officials invest in public goods and how trustworthy they are perceived to be. However, there does not seem to be an obvious link between how well village elections are implemented and how much villagers trust their leaders.

Table 4.8: Measures of local government performance

	No. of Observations	Village Public Goods Investment	Village Election Quality
Jiangsu	19	156.86	2.68
Sichuan	20	188.16	2.20
Shaanxi	16	112.61	1.75
Jilin	21	81.72	3.29
Hebei	18	66.04	2.28
Fujian	20	144.48	1.90
Sample	114	125.27	2.38

Source: CCAP Village Survey (2005)

4.4.3 Lineage Ties and Migration

Two contextual variables that may affect the development of self-governing organizations are lineage institutions and migration processes. Migration is measured by the proportion of the village labour force working outside the county in 2000. To avoid endogeneity concerns, this variable is also lagged one period. Migrants accounted, on average, for about 28 percent of the village labour force in 2000.

Lineage institutions are measured in three ways: (i) the type of clan structure; (ii) the nature of intra-clan relations; and (iii) the nature of inter-clan relations. First, following previous studies (e.g., Manion 2006), a village's lineage structure is measured by the proportion of households belonging to the three largest surname groups or, in other words, by the degree of surname concentration. 91 percent of the sample villages are multi-surname communities, and the average percentage of households belonging to the three largest surname groups was 56 percent (with a standard deviation of 27 percent) in 2004.

Second, and also in line with previous studies (e.g., Tsai 2007ab), the presence of active lineage groups and the degree of cohesion within clans in a village is measured by the number of ancestral halls which, as evidence from Fujian and Zhejiang shows, are “at the center of the social, political and cultural life of lineages and whole villages” (Svensson 2012: 157-158). About 23 percent of the sample villages had (at least) one ancestral hall in 2004.

Finally, the degree of cooperation or conflict between clan groups is measured by a dummy variable, the inter-clan tension index, which takes the value 0 if relations are cooperative, and 1 if they are conflictual. In around 74 percent of the sample villages, inter-clan relations were described as cooperative at the time of the survey, while in the other 26 percent they were considered somewhat conflictual (24%) or conflictual (2%).

4.4.4 Control Variables

The model controls for a number of economic, demographic and geographic factors that may affect participation in self-governing organizations. It includes a set of economic variables representing the level of village economic development, namely, the log of per capita net income, the amount of per capita farmland, as well as the number of collective, private, and individual (*getihu*) enterprises. Additionally, the model includes a set of demographic and geographic controls, in particular, the log of the village population, the proportion of flat land in the village, the log of the distance to the township, as well as provincial dummies.

4.4.5 Econometric Model and Estimation Method

To address potential problems of endogeneity, we specify a simultaneous equations model, with “political trust” and “participation in self-governing organizations” as the endogenous variables, and estimate it using three-stage least squares. For the model to be identified, we need (at least) two exclusion restrictions. One exogenous variable in the “participation” equation must be excluded from the “trust” equation, and vice versa. To this end, the variable “number of collective

enterprises” is excluded from the participation equation and included in the trust equation, while the variable “number of ancestral halls” is omitted from the trust equation and included in the participation equation.

The plausibility of these exclusion restrictions rests on two crucial assumptions. The first one is that the “number of collective enterprises” has a direct impact on political trust, but only an indirect impact on participation in self-governing organizations, through its effects on political trust. This assumption is reasonable. The presence or absence of collective enterprises in rural communities has been identified as the single most important determinant of the severity of the so-called “peasant burden” problem and the resulting conflict between villagers and officials over taxation issues (Benstein and Lü 2000, 2003, 2008).

The second assumption is that the “number of ancestral halls” has a direct impact on participation in self-governing organizations, but only an indirect impact on political trust (*via* participation in these organizations). This assumption also seems reasonable in light of evidence showing that lineage-based organizations, such as old people’s associations, often have their “centres” (Hansen 2008) or “offices” (Svensson 2012: 162) in ancestral halls.

In order to refine the model further, two additional exogenous variables are included in the first stage of the 3SLS estimations. These variables are: (1) the number of villagers who participated in the Anti-Japanese War (1937-45), the Liberation War (1945-49), and the Korean War (1950-53) under the leadership of the Chinese Communist Party; and (2) the number of villagers who were persecuted during the Cultural Revolution (1966-1976). These historical variables are clearly exogenous and, as pointed out by Tao et al. (2011: 115), may have influenced political attitudes in the Chinese countryside across generations. They may exert a direct impact on political trust, but only an indirect impact on participation in self-governing organizations, through their effects on political trust⁸⁶.

⁸⁶ There might be a positive relationship between the number of war veterans and the level of political trust in a village, and a negative relationship between the number of villagers persecuted during the Cultural Revolution period and the level of political trust. The first-stage results of the regression indicate that the number of war veterans has a positive significant impact on the level of political trust but has no significant (direct) impact on participation in self-governing organizations. This is shown in Table 4.10.

The simultaneous equations model and the main hypotheses are summarized in Table 4.9. As previously discussed, existing evidence suggests that there may be a two-way relationship between the endogenous variables (i.e., political trust and participation in self-governing organizations). This justifies the use of a nonrecursive simultaneous equations model (Table 4.9) to test our hypotheses on the determinants of participation in self-governing organizations. However, we also need to consider the possibility that there is a one-way relationship between these variables. Political trust may influence participation in self-governing organizations, but participation in these organizations may have no impact on the political attitudes of their members. For this reason, we also specify a recursive simultaneous equations model and estimate it using three-stage least squares.

Table 4.9 Political Distrust and Participation in Self-governing Organizations: Main Model Specification and Hypotheses

	Participation in self-governing organizations (Eq. 1)	Political trust (Eq. 2)
<i>Measure of political trust</i> • Political trust index at the village level (0-5)	-	n/a
<i>Measure of participation in self-governing organizations</i> • Participation rate in self-governing organizations	n/a	-
<i>(Time-Lagged) Measures of local government performance</i> • Ln (per capita village government investment in public goods) • Village election quality index (0-5)	-	
<i>Measures of clan structure and relations</i> • Percentage of households belonging to the three largest surname groups • No. of ancestral halls • Inter-clan tension index (0-1)	+	
<i>Measure of out-migration</i> • % migrants in village labour force	+	
<i>Economic controls</i> • Ln (per capita net income) • No. private enterprises • No. collective enterprises • No. self-employed businesses		
<i>Demographic and geographic controls</i> • Ln (village population) • Per capita arable land (mu) • Percentage of flat land • Ln (distance to the town, km)		
<i>Exogenous variables or instruments only included in the first-stage regression</i> • No. of war veterans • No. of villagers persecuted during the Cultural Revolution		
<i>Exclusion restrictions</i> • No. of collective enterprises (variable excluded from Eq. 1) • No. of ancestral halls (variable excluded from Eq. 2)		

4.5 Results and Findings

The results of the 3SLS estimation of the two-equation models are presented in Tables 4.10, 4.11 (nonrecursive model), and 4.12 (recursive model). Our main hypothesis – that lower levels of trust in grassroots officials lead to higher levels of participation in self-governing organizations – is confirmed. As can be seen in Tables 4.11 and 4.12, a one percent decrease in the political trust index is associated with a 0.65 (Table 4.11) or a 0.60 (Table 4.12) percentage point increase in the participation rate. The results in Table 4.12 also show that there is a reciprocal relationship between these two variables. Political distrust is both a cause and a consequence of participation in self-governing organizations. The fact that villagers form their own organizations to address community needs not only reflects, but also contributes to, their growing apathy and disengagement from the state.

The hypothesis regarding the impact of government performance on the development of self-governing organizations is partially supported. The results in Tables 4.11 and 4.12 (Eq. 1) indicate that the performance of government institutions does not affect participation in self-governing organizations directly, but indirectly through political trust (Eq. 2). They also indicate that public goods provision is the aspect of government that is most important in shaping villagers' perceptions about the trustworthiness of government officials. The coefficient on the public investment variable (Eq. 2) is positive and significant at the 5 percent (Table 4.12) or 10 percent level (Table 4.10) in the recursive and nonrecursive models. This suggests that villages with lower levels of government investment in infrastructure are also the villages with lower levels of political trust and, consequently, those with higher levels of participation in self-governing organizations.

In addition to institutional factors, social and economic factors also explain differences among villages in the extent of participation in these organizations. As can be seen in Tables 4.11 and 4.12, our hypotheses about the effects of clan structure and migration processes are largely supported by the results. The presence of cohesive and active lineage groups in a village – as measured by the number of village ancestral halls – has a positive and significant impact on participation in self-governing organizations. The coefficients on the surname concentration variable and

the inter-clan tension variable have the predicted negative sign but are not significant at conventional levels. Like lineage institutions, migration is positively and significantly associated with participation in self-governing organizations in both model specifications.

These latter results can be interpreted as evidence of the absence of good government and of the presence of social capital in communities with multiple clans and higher levels of (circular) rural-urban migration. On the one hand, our findings in Chapter 3 suggest that villages where a smaller number of households belong to the three largest surname groups and where a larger share of the labour force works outside the county receive less investment in infrastructure. On the other hand, the presence of clan and migration networks may enhance the ability of communities to provide themselves with the public goods that are under-provided by the state. These different forms of social capital may provide a means not only to prevent the opportunistic behaviour of community members, but also to access resources outside the community.

Regarding the effect of the control variables, the results show that, while the presence of self-employed households in a village has a significant negative impact on membership in self-governing organizations, the presence of larger private enterprises has the opposite effect. The causal mechanism by which these variables influence the development of self-governing organizations may be related to differences in the willingness and ability of self-employed individuals (*getihu*) and private entrepreneurs to make (time and money) contributions to these organizations. It may also be related to differences in political attitudes. There is evidence that villagers with higher incomes are more likely to believe that elected village committees should be autonomous from township governments and village Party branches and should be given the power to govern their communities (Tan and Xin 2007: 591).

To conclude, a comparison of the determinants of participation in self-governing and government-controlled organizations (see Table 4.11) highlights how the decline in political trust and the revival of traditional networks (i.e., clans) underpin the incipient development of autonomous associational life in Chinese rural communities.

Table 4.10: Results of the first-stage regression (nonrecursive model)

	Participation rate in self-governing organizations	Participation rate in govt.-controlled organizations	Average political trust
No of villagers persecuted during the Cultural Revolution	-84.875 (0.50)	60.351 (0.27)	-2.071 (0.91)
No of war veterans	-99.597 (1.20)	119.654 (1.08)	2.452 (2.22)**
Election quality index (last election before 2004)	0.245 (0.24)	1.117 (0.83)	0.011 (0.78)
Per capita village government investment in public goods (2003-04)	-96.264 (1.64)	84.142 (1.08)	1.310 (1.68)*
No. of ancestral halls	2.198 (3.37)***	-0.018 (0.02)	-0.013 (1.49)
% of households belonging to the three largest surname groups	0.036 (0.77)	-0.039 (0.62)	-0.001 (1.03)
Inter-clan tension index	-6.031 (0.55)	-1.134 (0.08)	-0.189 (1.29)
% of migrants in village labour force (2000)	0.222 (3.57)***	0.154 (1.85)***	0.001 (1.27)
No. of collective enterprises	-0.138 (0.06)	-2.320 (0.72)	0.020 (0.61)
% of self-employed households	-0.165 (1.46)	-0.002 (0.01)	-0.001 (0.39)
No. of private enterprises	0.186 (1.46)	0.197 (1.16)	0.001 (0.76)
Ln (per capita net income)	2.196 (0.84)	-7.284 (2.08)**	0.019 (0.54)
Per capita arable land	1.712 (0.12)	19.443 (1.00)	0.026 (0.13)
Ln (village population)	-0.548 (0.23)	5.120 (1.60)	0.052 (1.63)
% of flat land	0.056 (1.51)	-0.034 (0.68)	-0.001 (1.78)*
Ln (distance to the town)	-0.868 (0.58)	-3.331 (1.67)*	0.011 (0.57)
Constant	-21.553 (0.84)	29.935 (0.87)	-0.036 (0.11)
Provincial dummies	Yes	Yes	Yes
R ²	0.459	0.222	0.432
F test	3.72	1.25	3.33
[p-value]	[p = 0.000]	[p = 0.233]	[p = 0.000]
Observations	114	114	114

Note: Figures in parentheses are absolute values of t-statistics

* Significant at the 10% level

** Idem, 5%

*** Idem, 1%

Table 4.11: 3SLS estimates of the relationship between political distrust and participation in self-governing organizations (nonrecursive model)

	Self-governing organizations		Government-controlled organizations	
	Participation rate (Eq. 1)	Average political trust (Eq. 2)	Participation rate (Eq. 1)	Average political trust (Eq. 2)
Average political trust	-64.869 (3.20)***		50.977 (2.89)***	
Participation rate in self-governing org.		-0.009 (2.24)**		
Participation rate in govt.-controlled org.				0.019 (2.65)***
Election quality index (last election before 2004)	0.715 (0.76)	0.008 (0.62)	0.754 (0.58)	-0.014 (0.57)
Per capita village government investment in public goods (2003-04)	12.899 (0.22)	0.772 (0.95)	-15.439 (0.21)	0.283 (0.20)
No. of ancestral halls	1.000 (1.73)*		-0.009 (0.02)	
% of households belonging to the three largest surname groups	-0.0003 (0.01)	-0.0002 (0.30)	-0.007 (0.12)	0.0000 (0.12)
Inter-clan tension index	-17.753 (1.61)	-0.233 (1.52)	8.210 (0.56)	-0.161 (0.60)
% of migrants in village labour force (2000)	0.304 (4.65)***	0.003 (2.97)***	0.093 (1.11)	-0.002 (0.91)
No. of collective enterprises		0.007 (0.30)		0.005 (0.17)
% of self-employed households	-0.198 (1.87)*	-0.002 (1.12)	0.084 (0.60)	-0.002 (0.62)
No. of private enterprises	0.271 (2.23)**	0.003 (1.50)	0.167 (1.00)	-0.003 (0.94)
Ln (per capita net income)	2.833 (1.15)	0.028 (0.76)	-7.998 (2.35)**	0.154 (1.86)*
Per capita arable land	1.397 (0.10)	0.018 (0.09)	25.250 (1.36)	-0.484 (1.30)
Ln (village population)	3.815 (1.72)*	0.055 (1.85)*	1.507 (0.52)	-0.029 (0.49)
% of flat land	-0.005 (0.14)	-0.0004 (0.78)	0.020 (0.52)	-0.000 (0.43)
Ln (distance to the town)	-0.048 (0.03)	0.004 (0.21)	-4.1260 (2.11)**	0.080 (1.81)*
Constant	-26.030 (1.11)	-0.192 (0.52)	34.993 (1.08)	-0.671 (1.01)
Provincial dummies	Yes	Yes	Yes	Yes
R-squared	0.081	0.204	-0.15	-2.14
F test	4.78	3.31	2.30	1.81
[p-value]	[0.000]	[0.000]	[0.002]	[0.025]
Observations	114	114	114	114

Note: Figures in parentheses are absolute values of t-statistics

* Significant at the 10% level

** Idem, 5%

*** Idem, 1%

Table 4.12: 3SLS estimates of the relationship between political distrust and participation in self-governing organizations (recursive model)

	Self-governing organizations		Gov-controlled organizations	
	Participation rate (Eq. 1)	Average political trust (Eq. 2)	Participation rate (Eq. 1)	Average political trust (Eq. 2)
Average political trust	-59.724 (2.61)***		86.571 (2.82)***	
Election quality index (last election before 2004)		0.002 (0.18)		0.008 (0.74)
Per capita village government investment in public goods (2003-04)		1.424 (2.14)**		1.196 (1.89)*
No. of ancestral halls	1.306 (1.90)*	-0.012 (1.57)	1.147 (1.19)	-0.012 (1.54)
% of households belonging to the three largest surname groups	-0.003 (0.07)	-0.0004 (0.75)	0.005 (0.08)	-0.0000 (0.74)
Inter-clan tension index	-15.497 (1.32)	-0.175 (1.29)	15.869 (0.97)	-0.188 (1.39)
% of migrants in village labour force (2000)	0.294 (4.38)***	0.002 (2.10)**	0.043 (0.46)	0.002 (2.10)**
No. of collective enterprises	0.558 (0.23)	0.017 (0.58)	-4.644 (1.38)	0.023 (0.77)
% of self-employed households	-0.202 (1.82)*	-0.0003 (0.21)	0.042 (0.27)	-0.0000 (0.20)
No. of private enterprises	0.265 (2.03)**	0.001 (0.81)	0.090 (0.49)	0.001 (0.79)
Ln (per capita net income)	2.701 (1.05)	0.008 (0.25)	-8.650 (2.39)**	0.011 (0.33)
Per capita arable land	-0.673 (0.05)	-0.019 (0.11)	18.776 (0.93)	-0.004 (0.02)
Ln (village population)	3.391 (1.56)	0.046 (1.76)*	0.418 (0.14)	0.044 (1.68)*
% of flat land	-0.003 (0.08)	-0.0008 (1.82)*	0.044 (0.79)	-0.001 (1.84)*
Ln (distance to the town)	-0.053 (0.03)	0.011 (0.60)	-4.397 (2.06)**	0.011 (0.59)
Constant	-23.162 (0.94)	0.104 (0.34)	32.953 (0.94)	0.089 (0.29)
Provincial dummies	Yes	Yes	Yes	Yes
R-squared	0.140	0.394	-0.629	0.394
F test [p-value]	4.50 [p = 0.000]	3.94 [p = 0.000]	1.61 [p = 0.062]	3.91 [p = 0.000]
Correlation between participation rate and the error terms of political trust equation	r = -0.048 [p = 0.613]		r = -0.136 [p = 0.151]	
Observations	114	114	114	114

Note: Figures in parentheses are absolute values of t-statistics

* Significant at the 10% level

** Idem, 5%

*** Idem, 1%

4.6 Summary

Throughout the developing world, there are numerous examples of “substitutive informal institutions” (Helmke and Levitsky 2004) that have emerged in response to the ineffectiveness of formal institutions in providing public services in rural areas (e.g., Narayan 1999; Narayan and Walton 2000; Woolcock and Narayan 2000). “Rondas” in Peru (Muñoz et al. 2007), “harambees” in Kenya (Miguel and Gugerty 2005), and “informal panchayats” in India (Pur 2007) are just a few of them. Although informal institutions may fill the gap left by the state in the provision of rural infrastructure, education, health, and other basic services, they are often “poor substitutes” for formal institutions (Narayan 1999: 37). Worse yet, by substituting for the state in rural service provision, they may undermine its legitimacy and performance in rural areas, insofar as the two types of institutions compete to mobilize resources and support from rural residents (Cammet and MacLean 2011; Batley et al. 2012; Ali et al. 2014).

The goal of this chapter was to examine the rise of self-governing organizations in rural China and to assess their role and impact as (non-state) providers of basic infrastructure services. The analysis of survey data on 552 village organizations reveals that most of them were established by the state and have remained under its control. However, almost one-fourth of these community-based organizations are self-governing in that they are run by villagers, not by local officials.

Although self-governing organizations take a wide variety of forms, we found that the majority of them are either religious organizations, such as Buddhist temples or Christian churches, or lineage-based organizations, such as old people’s associations and wedding and funeral councils. Consistent with previous studies (Croll 1999; Tsai 2002, 2007ab, 2011), the survey data indicate that religious and clan organizations, which constituted “the most important organizational reality in rural society” in the pre-1949 period (Brandstädter 2003: 90), have re-emerged in rural areas, sometimes under new names, and often to perform their traditional roles as non-state service providers. In this respect, we found that around one-third of self-governing organizations were involved in the construction and maintenance of village infrastructure during the 2000-2005 period. While some of these associations

may be able to raise funds and carry out infrastructure projects independently without the support of the two village committees (e.g., local temples in Fujian), they have a limited capacity to fill the gap left by the state in the provision and maintenance of roads, drinking and irrigation water, and schools - the types of public goods to which villagers attach the highest priority (Yi et al. 2011: 120-122). This is most obvious among certain types of organizations, such as churches, and in poorer provinces, such as Shaanxi. For this reason, the formation of self-governing organizations can only be a second-best solution to the problem of underprovision of public goods in rural communities.

In addition to exploring the service delivery role of self-governing organizations, the main objective of this chapter was to examine the effects of various institutional, social and economic factors on villagers' participation in these organizations, including political trust, government performance, clan structure and migration processes. For this purpose, a two-equation simultaneous equations model, in which political trust and membership in self-governing organizations were the endogenous variables, was estimated using three-stage least squares.

Three major findings emerged from the results. First, whether villagers participate in government-controlled or self-governing organizations depends on how much they trust township officials. The more trustworthy villagers perceive township cadres to be, the more willing they are to join government-controlled organizations. Conversely, the less villagers trust township officials, the more likely they are to join self-governing organizations. While differences in government performance are associated with differences in the level of participation in self-governing organizations, the causal relationship between these two variables seems to be indirect and mediated by political (dis-)trust. More specifically, villages with lower levels of government investment in infrastructure are also the villages with lower levels of political trust and, consequently, those with higher levels of participation in this type of organizations.

These findings are consistent with those in Chapter 3. We found that, by increasing the influence of township officials over village governance, the cadre responsibility system makes village governments less democratically accountable to villagers, and village spending less responsive to public good needs. Specifically,

village governments that are less autonomous from, and more accountable to, township governments are less likely to be run by (democratically elected) village committees and are not more likely to invest in public goods. Villagers are aware of the extent to which, and the way in which, township officials influence how and by whom their communities are governed. This is why, in villages where township officials neither govern nor let others (i.e., village officials) govern in the interest of their residents, the latter may have strong incentives to form and participate in self-governing organizations as a means to disengage from the state and to address community needs independently from it.

Second, villages with more cohesive lineage groups and with larger migration networks provide a context conducive to the development of self-governing organizations. This may be for two reasons. The first one is related to a community's incentives for collective action. Our findings in chapter 3 and those of other studies show that villages in which a larger share of the population are migrants (Luo et al. 2010), and in which a smaller share of the population belongs to the largest surname group (Kung et al. 2009), invest less in infrastructure. Hence, it is in these communities where villagers are more likely to have strong incentives to participate in and contribute to social organizations that provide basic infrastructure services. The second reason is related to a community's capacity for collective action, which is itself affected by its "stock of social capital" (Putnam 1993, 2000), whether in the form of "intra-community ties" (i.e., "bonding social capital") or "extra-community networks" (i.e., "bridging social capital") (Woolcock 1998; Narayan 1999). Lineage ties and migration networks are types of "bonding" and "bridging" social capital (Woolcock 1998; Narayan 1999) and, as such, they can promote "integration" within rural communities while at the same time providing access to remittances and "linkages" to urban areas. Although in principle inter-clan conflicts and out-migration flows could create obstacles to successful collective action at the village level, our findings suggest that this is not the case, because inter-clan relations are often cooperative, and rural-urban migration is still predominantly circular.

Third, participation in self-governing organizations is not only a result but also a cause of the growing lack of trust in township officials. By reducing the legitimacy of rural governments, these organizations may further undermine their

capacity to govern effectively. Recent studies point in this direction. For example, it has been found that the presence of self-governing organizations has a negative impact on the ability of grassroots governments to raise revenues from villagers (Liu et al. 2012), and that (substitutive) non-state provision has a negative effect on the perceptions that grassroots officials have of their own authority and ability to implement government policies in rural communities (Tsai 2011). This suggests that presence of self-governing organizations may give rise to a vicious circle between weak state legitimacy and weak state capacity.

Overall, our findings on the rise and role of self-governing organizations in rural China speak to the literature on decentralization. They raise the question as to whether, by weakening the (downward) accountability of grassroots officials, the re-centralization of power within the Party-state may paradoxically lead to a “decentralization by default”⁸⁷ (Manor 1999), characterized by the resurgence of traditional community organizations, such as religious and clan-based organizations, in response to the service provision gap resulting from the unwillingness or inability of grassroots officials to meet local needs and demands. They also suggest that participation in self-governing organizations should be viewed as a symptom of poor local governance rather than as a solution to it, insofar as it reflects and contributes to the growing cleavage between citizens and officials in rural areas. This interpretation is consistent with the finding of other studies that it is “disengagement”, not “harmony”, what characterizes state-society relations in Chinese villages after the rural tax reform (Chen 2014: 725).

In rural China, as in the rural areas of other developing countries, the challenge is thus “to transform situations where a community's social capital substitutes for weak, hostile, or indifferent formal institutions into ones in which both realms complement one another” (Woolcock and Narayan 2000: 238). However, improving state-society relations in rural areas may require reforming central-local state relations in the first place. As Levi (1998: 87) reminds us, “trustworthy government actors are generally those who are embedded in trustworthy

⁸⁷ Manor (1999) and others (Davis et al. 1994; Olowu and Wunsch 2004) have used the term “decentralization by default” to refer to an “unintended” form of decentralization, in which non-state organizations at the grassroots level take over the role of the state in the provision of basic public goods and services.

institutions”. In China, building trustworthy institutions at the county, township and village levels may require promoting and consolidating, rather than preventing or reversing, the processes of political, fiscal and administrative decentralization. Arguably, unless rural officials are provided with adequate authority, resources and incentives to be responsive to villagers’ needs, they are unlikely to be, and to be perceived as, trustworthy. At the same time, in the absence of trust between societal and state actors, the pattern of interaction between informal and formal institutions in local governance is likely to be one of substitution rather than complementarity.

Chapter 5
Conclusion

5.1 Introduction

Decentralization is threatened when the wrong mix of powers is devolved, encumbering local authorities without giving them sufficient resources to be effective. It is threatened where non-representative or unaccountable actors are empowered, taking authority away from democratic actors or from the public arena. It is also threatened when local actors are so restrained by oversight that they have no room to act independently on behalf of local people. When local authorities cannot deliver goods or respond to local needs they cannot gain respect and legitimacy or engage local populations in public action. (Ribot 2002: 55)

Decentralization has long been advocated as a way of making government more “accountable” and “responsive” to the governed (Faguet 2012). However, despite these claims about the potential benefits of decentralization and a large literature examining its effects on the quality of governance and public services in the rural areas of developing countries, the empirical evidence remains mixed and inconclusive⁸⁸ (e.g., Rondinelli et al. 1983; Parker 1995; Crook and Manor 1998; Agrawal and Ribot 1999; Manor 1999; Blair 2000; Rosenzweig and Foster 2003; Francis and James 2003; Olowu and Wunsch 2004; Khemani 2005; Bardhan and Mookherjee 2006a; Tsai 2007b; Faguet and Sánchez 2008; Lu 2015). Decentralization has improved government accountability and rural service provision in some countries but not in others (e.g., Crook and Manor 1998), and in some regions or communities but not in others⁸⁹ (e.g., Lu 2015).

This lack of conclusive evidence is partly due to differences in the design and implementation of decentralization reforms across and within countries: countries and regions have decentralized in different ways and to varying degrees⁹⁰ (Parker

⁸⁸ For a comprehensive overview of the state of knowledge on decentralization see Faguet (2012: 179-191).

⁸⁹ Litvack et al. (1998: 30) have pointed out that “it is not much of an exaggeration to say that one can prove, or disprove, almost any proposition about decentralization by throwing together some set of cases or data”. For every study that finds a positive relationship between decentralization and service provision (e.g., Estache and Sinha 1995; Parker 1995; Besley and Burgess 2002; Rosenzweig and Foster 2003; Eckardt 2008; Faguet 2008), or a negative relationship between decentralization and corruption (e.g., Huther and Shah 1998; Fisman and Gatti 2002), there is another study which finds no, or even the opposite, relationship (e.g., Francis and James 2003; Akin et al. 2005; Khemani 2005; Fan et al. 2009).

⁹⁰ Another reason for the lack of conclusive evidence is that we should not have expected to find it in the first place, given that the outcomes of decentralization are contingent on contextual factors (e.g., Bardhan and Mookherjee 2006a; Ahmad and Brosio 2009; Faguet 2012).

1995; Ribot 2002; Azfar et al. 2004; Yilmaz et al. 2010). At the same time, existing studies suggest that decentralization is unlikely to lead to better government performance unless: (i) it entails a mixture of political, fiscal, and administrative decentralization (Manor 1999; Parker 1995); (ii) it takes the form of devolution, rather than that of deconcentration or delegation (Olowu and Wunsch 2004; Bardhan and Mookherjee 2006a); and consequently (iii) it implies that “powers and resources are transferred to authorities representative of and downwardly accountable to local populations” (Ribot 2002: ii). These same studies suggest that, in much of the developing world, decentralization reforms have ultimately failed to make elected local governments more accountable to citizens for the provision of services because they have failed to devolve power and resources to them in the first place (e.g., Parker 1995; Crook and Manor 1998; Ribot 2002; Olowu and Wunsch 2004; Bardhan and Mookherjee 2006a; Faguet 2012). China does not seem to be an exception.

The analysis of the political, fiscal, and administrative dimensions of decentralization at the village level reveals what we have called “the accountability-power paradox” in village governance: villagers have more – and seemingly more effective – mechanisms to hold village committees accountable, but village committees have less, if any, power to govern. This study has investigated some of the possible reasons behind this paradox, including the centralization of the fiscal and administrative systems, as well as its implications for accountability and participation in local governance and public goods provision in rural communities. More specifically, it has examined how the recent turn towards centralization in China has affected the “voice” and “exit” options (Hirschman 1970) available to villagers for improving public goods provision in their communities, by addressing two main questions. The first question investigated was, whether, by shifting power away from village committees and towards county, township, and village-level Party committees, recent fiscal, administrative and political reforms have undermined the effectiveness of village-level democratic institutions and, thereby, constrained the ability of villagers to use the “voice” option to create incentives for rural officials to meet their demands for public goods and services. The second question examined was, whether, when state institutions fail to meet local needs and demands and, by extension, fail to elicit “loyalty” (i.e., trust), villagers choose to “exit” from state

provision to non-state provision through the formation of social organizations that take over responsibility for the provision of basic infrastructure services in their communities. In the remainder of the chapter, we summarize the main findings and contributions of our research.

5.2 Main Findings

5.2.1 The “Accountability-Power Paradox” in Village Governance

Recent legal, fiscal, administrative and political reforms reflect the reluctance of the central government and, especially, of intermediate governments to devolve power to villages and, within villages, to democratically elected village committees. First, the 2010 Organic Law of Village Committees remains ambiguous regarding the division of power and functions between village committees, on the one hand, and township and village Party organizations, on the other (e.g., Alpermann 2013). Second, the elimination of agricultural taxes and fees has sharply reduced the amount of resources over which village governments have control or discretion, limiting the scope of what they can do and be held accountable for (e.g., World Bank 2007; Fock and Wong 2008; Tian 2009; Oi et al. 2012; Takeuchi 2014). Third, the adoption of the so-called “cadre-in-residence” and “salaries-from-above” policies (Oi et al. 2012; Smith 2010) has reduced the autonomy of village officials vis-à-vis their Party superiors and transformed village governments into “outposts of township governments” (Smith 2010: 614). Last but not least, the introduction of elections for village Party secretaries has helped to legitimize and thus to reinforce their dominant position in village governance (Sun et al. 2013).

The implementation of these fiscal, administrative and political reforms represents a clear shift in China’s (de-)centralization policies. By shifting power away from village committees towards county, township and village-level Party committees, these reforms may have undermined the effectiveness of village elections and other mechanisms of external accountability and may have created an “accountability gap” in village governance that cannot be filled by internal

mechanisms of accountability alone, whether fiscal (e.g., earmarked transfers), administrative (e.g., performance contracts) or political (e.g., intra-Party elections).

However, at the same time, there is evidence of differences in the implementation implications of these reforms across villages. Villages have not become equally dependent on fiscal transfers to provide public goods (e.g., Takeuchi 2014), nor are they subject to the same degree of bureaucratic control (e.g., Smith 2010; Oi et al. 2012; Sun et al. 2013), and nor do they (s)elect their Party leaders in the same way (e.g., Sun et al. 2013)⁹¹. Furthermore, they still differ in the quality of their elections and in the distribution of power between their village and Party committees (e.g., O'Brien and Zhao 2011; Sun et al. 2013). The evidence points to the emergence of a variety of local governance systems that differ in at least two key respects: (i) the nature of and interrelationships among the political, fiscal and administrative dimensions of (de-)centralization at the village level; and (ii) the relations of power and accountability among villagers, village committees, village Party branches and higher-level governments.

Against this background this study aimed to assess the potential and limits of political decentralization as a means to improve local governance and local public goods provision in the context of an authoritarian and (fiscally and administratively) centralized state. It raised three main questions: (i) whether political decentralization – if and where it has occurred – has resulted in a better provision of public goods by village governments; (ii) whether the implementation of the fiscal, administrative and political reforms outlined above has undermined political decentralization, and in what ways; and (iii) whether accountability in the provision of public goods can be achieved without political decentralization or, in other words, whether earmarked

⁹¹ For instance, research by Takeuchi (2014: 186) shows that “although rural tax reforms (...) were introduced universally in China, their implementation and effects on rural governance varied from area to area”. They had a particularly negative impact in poor agricultural areas, where local governments became trapped in a vicious circle: on the one hand, they “lost revenue sources, struggled to cover administrative costs, and were unable to provide public goods”. On the other, they “lost the authority to govern their localities as villagers blamed local governments for the lack of public goods and the declining quality of rural governance” (Takeuchi 2014: 86). Recent research by Sun et al. (2013), Oi et al. (2012) and Smith (2010) also shows that there are significant variations across villages and provinces in terms of: the dependence of township cadres on village officials to meet their performance targets under the cadre evaluation system (Sun et al. 2013); the number of township officials that work as “sent-down” cadres in villages under the “cadre-in-residence” policy (Smith 2010; Oi et al. 2012); and the type of procedure by which village Party secretaries are (s)elected (Sun et al. 2013).

transfers, performance contracts, and intra-Party elections can be a good substitute for village-level elections and other democratic institutions.

In line with these questions, this study examined empirically: (i) whether variation in political decentralization across villages explains variation in their investment in infrastructure (i.e., village-financed investment); (ii) whether and how variation across villages in the degree of transfer dependence (i.e., government-financed investment), top-down Party control (i.e., the cadre responsibility system), and intra-Party democracy (i.e., intra-Party elections) is associated with variation in the degree of political decentralization (i.e., village democratic reforms)⁹²; and (iii) whether and how variation across villages in the degree of top-down Party control, and intra-Party democracy is associated with variation in the level of village-financed investment in infrastructure.

Two simultaneous-equation models of “village democracy” and “local public goods provision” were estimated using cross-sectional data for 115 villages from the Center for Chinese Agricultural Policy Village Survey (2005). The main dependent variable in the first model was “village-financed investment”, while in the second model it was “government-financed investment”. Measures of the implementation of the cadre responsibility system and the intra-Party election system were included as exogenous variables in each of the models. Both were estimated using three-stage least squares.

Two main findings emerged from the empirical analysis. The first finding is that villages where (i) elections are better implemented, and where (ii) popularly elected village committees (leaders) have control over village finances, tend to invest more in infrastructure (i.e., village-financed investment). However, at the same time, they seem to receive a smaller share of (capital) grant funds from higher-level governments (i.e., government-financed investment). This suggests that whether village elections matter (or not) for public goods provision crucially depends on: (i)

⁹² The underlying question was: (i) whether the cadre responsibility system creates perverse incentives for township officials to obstruct village democratic reforms; (ii) whether the intergovernmental transfer system leaves room for county and township governments to target more resources to politically favoured villages, namely, those where the village Party branch remains the dominant governing body; and (iii) whether the implementation of intra-Party democratic reforms justifies or legitimizes the lack of progress in the implementation of village democratic reforms. In other words, the use of performance contracts, intergovernmental transfers and intra-Party elections as mechanisms of accountability in rural governance may subvert rather than reinforce village democratic institutions.

who finances village infrastructure projects – the village or higher-level governments – and (ii) who controls village finances - the village committee and/or the Party branch. When local spending decisions are made by village Party branches (i.e., village-financed investment) or by county and township Party committees (i.e., government-financed investment) the potential positive relationship between village elections and public goods provision either disappears or is reversed. There are two possible reasons. The first one is that, under such conditions, village elections do not provide a mechanism for villagers to ensure accountability in public goods provision because power over spending decisions has not been devolved to village committees. The second one is that earmarked grants might provide a mechanism for higher-level officials to target more resources to less democratic villages, that is, those governed by village Party organizations rather than by popularly elected village committees.

A second finding is that the cadre responsibility system and intra-Party elections have different effects on local governance and local public goods provision. Consistent with previous studies (Tsai 2007b; Sun et al. 2013), we found that tighter township control over villages is not positively associated with local public goods provision (i.e., village-financed investment), but it is negatively associated with local democracy. Village governments that are less autonomous from township Party committees are less likely to be run by popularly elected officials, while they are not more likely to invest in public goods. In contrast, the election of village Party secretaries by village Party members (without the interference of township officials) has a significant positive impact on local public goods provision (i.e., village-financed investment) and does not have a significant negative impact on local democracy. This latter finding is in contrast to that of Sun et al. (2013), who found that intra-Party democracy undermines village democracy, and calls for further research.

Taken together, our empirical findings point to the lack of a coherent framework for government accountability at the village level, where the political, fiscal, and administrative dimensions of decentralization tend to conflict with, rather than complement, one another. Our findings can be interpreted as follows: (1) political decentralization has a positive impact on the financing and provision of public goods by village governments; (2) the processes of political decentralization

and intra-Party democratization can complement one another in making village officials more (downwardly) accountable to villagers and Party members for the use of funds over which they have control or discretion; (3) administrative and fiscal centralization have a negative impact on political decentralization and compromise its potential benefits, mainly by reducing the power and autonomy of democratically elected village committees; and last (4) centralized bureaucratic and fiscal control may be poor substitutes for democratic accountability, given that (i) (earmarked) transfers can be used to distribute patronage to politically favoured villages, where power remains concentrated in the hands of Party organizations (i.e., government-financed investment); and that (ii) performance contracts are not used to create strong incentives for Party officials to invest in public goods (i.e., village-financed investment).

These findings make two contributions to the literature on political decentralization and public goods provision in rural China. The first contribution is to shed light on the conditions under which village residents can and do use elections to hold their leaders to account for the use of public funds. They show that a critical determinant of the effectiveness of village elections in ensuring accountability in public goods provision is not only whether villagers are given (electoral) control over village committees (i.e., the quality of village elections), but more fundamentally whether village committees are given control over fiscal resources (i.e., the power of village committees). This provides an answer to the puzzle of why relatively well-run elections often fail to deliver better governance and public goods provision. The answer (or part of it) lies in the local power structure: in most villages, village committees remain powerless. The problem with political decentralization in China is not that it does not work but that it has not taken place.

To date, the empirical literature on village elections disagrees on whether they provide an effective mechanism for villagers to hold grassroots officials accountable for the quality of service provision (Zhang et al. 2004; Luo et al. 2007, 2010; Tsai 2007ab; Wang and Yao 2007; Sato 2008; Kung et al. 2009; Meng and Zhang 2010; Martinez-Bravo et al. 2011; Mu and Zhang 2014; Lu 2015). Some studies argue that introducing direct elections for village committees is in itself sufficient to improve accountability in village governance (e.g., Luo et al. 2007, 2010), while others argue

that it is neither necessary nor sufficient (e.g., Tsai 2007ab). Our findings suggest that village elections are necessary but far from sufficient to address the problem of political accountability in rural communities. They show that their effectiveness is contingent upon the power structure in which village committees are embedded: only if village committees are given the power to govern (i.e., control over resources), can (free and fair) elections be expected to deliver accountability.

A second contribution of this study is to identify some of the obstacles to political decentralization or, in other words, some of the reasons for its poor implementation. The empirical results show that the potential benefits of political decentralization in terms of making village committees more accountable to villagers are compromised by processes of fiscal and administrative (re-)centralization that shift power away from village committees. We found that villages that are tightly controlled by township governments and that finance a greater share of their expenditures from transfers are less likely to be governed by popularly elected village committees. Hence, as O'Brien and Han (2009: 376) have pointed out, "(...) the quality of democracy in much of the countryside remains stubbornly low, mainly because VCs [village committees], once an election is over, are situated in a socio-political environment that has changed surprisingly little". Indeed, our research suggests that the reform of the fiscal and administrative systems has been instrumental in preventing political change at the grassroots level. Bureaucratic and fiscal institutions (i.e., the cadre responsibility system and earmarked transfers) provide more *incentives* and *means* for local Party officials at various levels to undermine grassroots political reforms⁹³.

⁹³ The cadre responsibility system still creates perverse incentives for township officials to resist the implementation of local democratic reforms, while the new intergovernmental transfer system leaves room for township Party committees to target more resources to less democratic villages.

5.2.2 *Non-State Provision by Self-Governing Organizations: “Decentralization by Default”?*

Despite the implementation of the rural tax reform, it has become increasingly difficult for grassroots officials to collect (legal) taxes and fees (Liu et al. 2012: 194) and, even more, to raise voluntary contributions from villagers to provide public goods and services (e.g. Chen 2008, 2014, 2015; Fock and Wong 2008; Tian 2009; Göbel 2010; Boyle et al. 2014). This seems to be particularly the case in villages where “self-governing organizations” have become a “substitute” for the (local) state in the provision of basic goods and services (Liu et al. 2012: 202).

This finding raises questions about the interactive relationship between levels of (local) state legitimacy and capacity, on the one hand, and forms of community participation and non-state provision, on the other, that this study sought to answer: What explains participation in self-governing organizations? What forms do they take? To what extent are they able to substitute for the (local) state in the provision of basic infrastructure? And what implications does this have for its legitimacy and ability to govern rural communities effectively?

If our sample villages are representative of China’s villages, there are reasons to believe that self-governing organizations are present in a majority (55%) of them. These voluntary organizations have two distinctive features: (i) they are run neither by local officials nor by their appointees but by villagers, and (ii) they do not incorporate local officials in their activities or decision-making processes. Although they take a wide variety of forms, we found that most of them are either religious organizations, such as Buddhist temples or Christian churches, or lineage-based organizations, such as old people’s associations and wedding and funeral councils.

We also found that, during the 2000-2005 period, around one-third of self-governing organizations were involved in the construction, repair and maintenance of village roads and bridges, drinking water and irrigations systems, as well as primary school buildings - the types of public goods that villagers care most about, and that are often under-provided by the state (Luo et al. 2010; Yi et al. 2011). As shown by other studies (Liu et al. 2012), self-governing organizations are less likely than other organizations to participate in the co-production of public goods with local officials, and more likely to engage in what is called “substitutive public goods

provision” (Tsai 2011), however we found that there are differences among them in terms of their role as non-state providers. While some organizations in some provinces have the capacity to raise sufficient funds from villagers to build, repair and/or maintain village infrastructure independently (e.g., local temples in Fujian), others lack the capacity to fill the gap left by the state in the provision of basic infrastructure services. This is especially the case among certain types of organizations, such as churches, and in poorer provinces, such as Shaanxi.

Against this background, this research sought to identify both the determinants and consequences of the growth of self-governing organizations and non-state provision in rural communities, with a focus on the issues of (local) state legitimacy and capacity. To this end, we first examined whether differences among villages in the level of participation in self-governing organizations are explained by differences in: (i) the level of trust between villagers and township officials; (ii) the amount of investment in village infrastructure; (iii) the quality of village elections; and (iv) the nature of the socioeconomic structure. Additionally, we examined whether and how participation in self-governing organizations affects trust between village residents and township officials.

A simultaneous equations model of “political trust” and “membership in self-governing organizations” was estimated by three-stage least squares, using survey data from 115 villages collected by the Center for Chinese Agricultural Policy in 2005. Measures of (i) village-financed investment (lagged), (ii) village election quality (lagged), (iii) rural-urban migration (lagged), as well as (iv) clan structure and intra-clan and inter-clan relations, were included in the main model as exogenous variables. To account for the possibility that there is a one-way relationship between political trust and participation in self-governing organizations and that they are both influenced by government performance, our hypotheses on the determinants of participation in these organizations were also tested using a recursive simultaneous equations model, which was estimated by three-stage least squares.

Two main findings emerged from the analysis. The first one is related to the determinants of participation in self-governing organizations. We found that the amount of participation in this type of organizations is largely a function of the amount of trust villagers have, or do not have, in township-level cadres: the less

trustworthy township officials are (or are perceived to be), the more likely villagers are to form and join self-governing organizations. Government performance – as measured by the amount of investment in village infrastructure and the quality of village elections – does not have a direct impact, but an indirect impact on the development of self-governing organizations. First, while differences among villages in the level of government performance are associated with differences in the level of participation in these organizations, the causal relationship between these variables seems to be mediated by political (dis-)trust. Second, the level of public goods provision, rather than the quality of village committee elections, appears to be the dimension of government performance that influences villagers' perceptions about the trustworthiness of government officials.

These results need to be interpreted in the context of the wider trend towards the centralization of power within the local Party-state. Township officials can and do influence how and by whom villages are governed – whether through formal channels (e.g., allocating transfers to villages, setting performance targets for village officials, working as “sent-down” cadres in villages, etc.) or informal ones (e.g., manipulating elections for village committees and Party branches). However, at the same time, they are neither elected by nor (directly) accountable to villagers. Furthermore, our finding that villages that are subject to greater (bureaucratic) control by townships are less likely to be governed by (democratically elected) village committees, but are not more likely to invest in public goods, suggests that township officials are not themselves held accountable by county officials for the quality of village governance and village public goods provision under the cadre responsibility system. This implies that in villages where township officials neither govern nor let others govern (i.e., village officials) in the interest of their residents, the latter are more likely to organize independently in order to cope with community needs. Our results indicate that the lack of trust in township officials creates incentives for villagers to form their own organizations and to cooperate among themselves in the provision of the goods and services that are under-provided by the state.

However, one thing is that villagers have an incentive to engage in these forms of collective action, and another is that they have the capacity to do it. In this

respect, we found that villages with (i) more cohesive lineage groups – proxied by the number of village ancestral halls - and with (ii) larger migration networks – as measured by the proportion of the village labour force working outside the county – tend to have higher levels of participation in self-governing organizations. This finding is consistent with the social capital literature, which stresses the importance for rural development of what is called “bonding” and “bridging” social capital (e.g., Narayan 1999), or “intra-community ties” and “extra-community networks” (e.g., Woolcock 1998), that is, different types of social networks at the community level that promote “integration” within the community, while providing “linkage” to resources outside the community. Although inter-clan conflicts and out-migration flows could prevent successful collective action in rural communities, our research suggests that this is not the case because inter-clan relations are often cooperative, and rural-urban migration is predominantly circular. In fact, the presence of clan networks and migration networks can provide a means to (i) foster cooperation and prevent opportunistic behaviour among community members; and to (ii) access resources otherwise unavailable to them (e.g., transfers, self-organization skills, etc.) – all of which is crucial to the development and role of self-governing organizations as non-state providers of basic goods and services in rural areas.

A comparison of the determinants of participation in self-governing and government-controlled organizations sheds further light on the institutional sources of variation across rural China in the form that non-state organizations and non-state provision take. Two differences stand out. First, political trust has a significant positive impact on participation in government-controlled organizations, but exerts a significant negative impact on participation in self-governing organizations. Second, clan solidarity exerts a significant positive effect on participation in self-governing organizations but has no significant effect on participation in government-controlled organizations. This lead us to conclude that the decline in trust in local political institutions (i.e., township governments) together with the revival of traditional social institutions (i.e., clans) are the single most important factors explaining the development of self-governing organizations in rural communities.

Our second main finding is related to the consequences of non-state provision by self-governing organizations for (local) state legitimacy. The empirical results

show that there is a reciprocal relationship between political trust and participation in self-governing organizations. In other words, the rise of these organizations is not only a consequence but also a cause of the growing lack of trust in township officials and, more generally, of the declining legitimacy of the (local) state. The fact that villagers form their own organizations to address community needs not only reflects, but also contributes to, the growing cleavage between state and society at the village level. This is consistent with and complements the findings of recent research showing that (i) participation in self-governing organizations is negatively associated with the “extractive capacity” of grassroots governments (Liu et al. 2012: 191); and that (ii), unlike other forms of non-state provision (e.g., co-production), “substitutive public goods provision” by community organizations is positively related to “village officials’ perceived difficulty in completing tasks assigned by higher levels” (Tsai 2011: 61). Taken together, these findings can be interpreted as evidence that non-state provision by self-governing organizations negatively affects two key dimensions of (local) state capacity – the capacity to tax (Liu et al. 2012) and to elicit compliance with state policies (Tsai 2011) –, through its negative effects on (local) state legitimacy.

Two main conclusions can be drawn from these findings. First, the centralization of power in the hands of officials that cannot be held to account by villagers for meeting their needs is leading in some areas to a “decentralization by default” (Manor 1999), characterized by the resurgence of traditional grassroots organizations, such as religious and clan-based organizations, to meet the needs for goods and services that are unmet by the state. There is evidence that recent re-centralization reforms have created a “vacuum in village administration” (Chen 2015), especially in agricultural regions. For instance, Chen (2015: 230) describes, how as a result of the implementation of the rural tax reform, village cadres “(...) found that they had no (major) functions to perform, no authority to govern, no capacity to undertake tasks, and no motivation to work” (Chen 2015: 230). Our findings suggest that in some parts of rural China, this vacuum has been partly filled by self-governing organizations. Second, as “substitutive informal institutions” (Helmke and Levitsky 2004), self-governing organizations are only a “second-best solution” to the problem of under-provision of public goods in rural communities.

In some cases these community organizations play a negligible role as providers of infrastructure services, while in others the fact that they succeed in providing services independently from the (local) state further undermines its legitimacy and, as a result, its capacity to tax and govern. In brief, self-governing organizations appear to be an ineffective *response* to “government failure” in poorer villages, while they may become a *source* of “government failure” in richer ones.

This study fits into a growing body of literature on the role of community organizations in local governance and local public goods provision in Chinese villages (e.g., Tsai 2002, 2007ab, 2011; Hansen 2008; Kung et al. 2009; Thogersen 2009; Lu 2015; Xu and Yao 2015). One of its main contributions is to rethink the way in which state and societal actors interact in village governance. Previous studies on this topic have stressed that the presence of community organizations in which local officials participate may enhance the performance of local governments (e.g., Tsai 2007ab; Lu 2015; Xu and Yao 2015). While we also examine the interactive relationship between community participation and local government performance, we emphasize the opposite direction of their causal relationship, that is, how the quality of local government affects the types of organizations villagers join and contribute time and money to. It highlights the need and the challenge of creating a relationship of complementarity between state and non-state actors in the context of public goods provision in the absence of trustworthy (local) state institutions, that is, institutions that have the necessary authority and resources to govern, and that can be held accountable by rural residents for their performance.

5.3 Contributions to the “Varieties of Governance” Literature

(...) it is no longer possible to find a stereotyped or regular pattern regarding whether and how cadre power works in villages. Instead, rural reforms over the past three decades – especially the recent RTR [rural tax reform] and the AAT [abolition of agricultural taxes] – have given rise to a variety of different ways in which cadres govern their villages. Political authority has mostly, if not entirely, evaporated in some villages and has turned into a source of tension and protest in some others. Still, in quite a few villages, cadres have retained or regained enough authority for them to govern effectively. (Chen 2015: 136)

A new literature on “varieties of governance” in rural China (Lu 2015) has emerged to explain variation in the quality of public goods provision across villages. As some have noted (Lu 2015: 3), few studies within this literature have tried to establish a comprehensive theoretical framework that helps us understand the institutional determinants of “good” government at the village level. Two notable exceptions are the studies by Tsai (2007ab) and Lu (2015). Both studies seek to explain why some village governments provide more public goods than others, by examining how – and how effectively - they address the “collective action problem” and the “accountability problem” associated with state provision (Tsai 2007a: 356-357, 2007b: 12-19; Lu 2015: 84-131).

Tsai develops a “model of informal accountability” (Tsai 2007a: 356-357; Tsai 2007b: 86-119), which posits that “villages with village-wide solidary groups that incorporate the participation of local officials are more likely to have a better governmental performance and public goods provision than villages without these groups” (Tsai 2007b: 20). Based on survey and case study data collected between 1999 and 2002 from a sample of more than 300 villages in the provinces of Fujian, Hebei, Jiangxi and Shanxi, her research finds that “encompassing and embedding solidary groups”, such as village-wide lineages, improve local governance and public goods provision by increasing “mutual accountability” between villagers and officials (Tsai 2007b: 166). In communities with these groups, officials are more likely to feel a strong social obligation to respond to villagers’ demands for public goods, which in turn makes villagers more willing to pay taxes and to make (monetary and labour) contributions to public projects. Her research also finds that local democratic reforms have failed to make village governments more accountable

to villagers, presumably due to the structural weaknesses of local elections as mechanisms of accountability: “(...) even in villages with extremely good implementation of democratic reforms, citizens do not necessarily have a great deal of leverage over officials, accurate information about their activities, or a particularly strong sense of civic duties” (Tsai 2007b: 190). In her view, the strengthening of local democratic institutions is not a *conditio sine qua non* for the development of accountable local governments: “we can have accountability without formal democracy if we have the right kinds of social groups (...)” (Tsai 2007b: 257). It is the presence of “encompassing and embedding solidary groups” that explains the emergence of “pockets of good governance” in parts of rural China (Tsai 2007b: 267).

Like Tsai (2007ab), Lu (2015) compares the role of formal institutions (i.e., village elections) and informal institutions (i.e., clans) in creating incentives for villagers to comply with taxation (i.e. the “collective action problem”) and for village officials to use public funds responsibly (i.e., the “accountability problem”). In his view, informal institutions (i.e., lineages) are neither intrinsically superior nor inferior to formal institutions (i.e., elections) in leading villagers and village officials to work together for the public good: “In some villages only indigenous relation-based institutions work; in other villages, only rule-based institutions function; and, still in other villages, neither indigenous nor imposed institutions work well” (Lu 2015: 109).

To explain this finding, he develops a model of public goods provision, which argues that the (relative) effectiveness of “indigenous relation-based institutions” (i.e., clans) and “imposed rule-based institutions” (i.e., elections) to overcome the “collective action” and “accountability” problems associated with state provision is contingent on a community’s level of outward migration and, as a result, varies across the spectrum of what he calls “close-knit”, “loosely coupled” and “atomized” communities.

Using survey data collected in 2008 from more than 300 villages in Henan, Hubei, Shandong and Shanxi, his research finds that rural-urban migration processes affect public goods provision in rural communities, through their effects on the performance of informal and formal institutions in preventing opportunistic

behaviour by villagers and village officials. Lu (2015) argues that informal institutions (i.e., lineages) facilitate public goods provision in “close-knit” communities, and that so do formal institutions (i.e., elections) in “loosely coupled” villages. However, in “atomized” communities, where out-migration is highest, neither informal nor formal institutions can address problems of poor local governance and inadequate public goods provision effectively. Hence, from his perspective, it is rural-urban migration that is mainly responsible for the emergence of pockets of poor governance in the Chinese countryside.

A close-knit social environment – more specifically, frequent and continuous social interaction and the existence of dense and extended social networks – favors the operation of indigenous relation-based institutions, while imposed rule-based institutions enjoy an advantage in loosely coupled communities. In contrast, in atomized communities, neither can work effectively as the institutional foundation of local governance. (Lu 2015: 9)

As can be seen, the two most recent and comprehensive studies on the emergence of “varieties of governance” across the Chinese countryside provide different answers to the question of why some village governments provide more public goods than others. For Tsai (2007ab), the key to explaining variation in village government performance lies in *social institutions* (i.e., encompassing and embedding solidary groups), while for Lu (2015) it lies in *economic institutions* (i.e., rural-urban migration).

Our research contributes to this new literature on the institutional determinants of “good” government at the village level in three ways. Its main contribution is to shift the analytical focus from economic and social institutions to *political institutions* in order to account for variation in local government performance in rural China. Based on survey data collected by the Center for Chinese Agricultural Policy in 2005 from more than 100 villages in Jilin, Shaanxi, Hebei, Jiangsu, Fujian, and Sichuan, our research finds that, in villages where democratically elected village committees have the power to govern, village officials tend to be more responsive to the demands of village residents for investment in basic infrastructure, such as village roads and bridges, drinking water and irrigations systems, and schools. It provides the basis for the development of a model of public goods provision by village

governments, in which the ability of village elections to solve the “collective action” and “accountability” problems associated with state provision is contingent not only on the quality of the electoral process but also on the power of the elected village committee (leader), that is, on the effective implementation of political decentralization. It contends that, in villages where elections are better implemented, and where elected village committees (leaders) have the power to govern (i.e., control over fiscal resources), their leaders are better able and more willing to mobilize resources from villagers to invest in public goods: they have a mandate and incentive to improve community infrastructure and services.

Our study thus suggests that the key to explaining variation in village government performance lies in the uneven implementation of political decentralization reforms across villages. The reason why some village governments perform better than others in providing public goods is because they have become what Gilley (2010) calls “democratic enclaves” in an authoritarian regime. In these villages, grassroots democratic institutions provide meaningful opportunities for villagers to voice their demands and to hold village officials accountable for meeting them. Hence, in our view, it is the emergence of “democratic enclaves” (Gilley 2010) that explains the existence of islands or pockets of good governance in parts of rural China.

Our research makes two additional contributions to the “varieties of governance” literature: it identifies some of the institutional causes and consequences of poor governance in rural areas. Research by Tsai (2007ab) and Lu (2015) suggests that poor governance is mainly a function of two local contextual factors, namely, the absence of (encompassing and embedding) solidary groups and the existence of out-migration. In its analysis of the causes of poor governance, our research shifts the focus of analysis from the community context to changes and variation in the implementation of (de-)centralization policies. It finds that one of the main obstacles to “good governance” lies in the tension between, on the one hand, the process of political decentralization and, on the other, the processes of fiscal and administrative (re-)centralization.

Our research shows that political decentralization has only taken place in a minority of villages (i.e., “democratic enclaves”). In a majority of them, elected

village committees have been established but remain powerless, while power has been delegated to governing bodies that are, at best, only upwardly accountable to higher levels of the Party-state (i.e., county-, township- and village-level Party committees)⁹⁴. It also suggests that variation in the degree of fiscal and administrative centralization across villages is negatively associated with the degree of political decentralization: villages with less fiscal and administrative autonomy from townships are less likely to be governed by democratically elected village committees. While more research is needed, our findings suggest that the centralization of the fiscal and administrative systems has created new obstacles to political decentralization. State and party actors who oppose political decentralization, such as township officials, can now use the intergovernmental transfer system and the cadre responsibility system in ways that undermine the “demand” and “supply” of local democratic reforms (Kennedy 2010a) – whether by allocating a smaller share of (earmarked) transfers to villages where political decentralization has gone furthest, or by interfering in village governance and not giving democratically elected village committees the autonomy and authority needed to govern. In brief, one of the main obstacles to political decentralization and the potential governance benefits it brings lies in the fiscal and administrative aspects of the intergovernmental system.

A last contribution of this study to the literature on “varieties of governance” is to identify some of the institutional consequences of poor governance in the Chinese countryside. Our findings suggest that variation in the quality of governance across villages partly explains variation in the forms that non-state organizations and non-state provision take. In the absence of good governance, villagers are less willing to participate in community organizations that are run by local officials or their appointees (i.e., government-controlled organizations), and to provide public goods in collaboration with the (local) state (i.e., co-production). Instead, they are more likely to form their own organizations (i.e., self-governing organizations) and to

⁹⁴ This situation is common in developing countries. For instance, according to Ribot (2002: 3), “many reforms are taking place in the name of decentralization, but they are not setting up the basic institutional infrastructure from which to expect the positive outcomes that decentralization promises. Instead, local democracies are created but given no power, or power is devolved to non-representative upwardly accountable local authorities”.

provide themselves with the public goods that the (local) state under-provides (i.e., self-provision or substitutive non-state provision).

More specifically, this study finds evidence that the decline in trust in formal institutions (i.e., township governments), together with the (re-)emergence of traditional informal institutions (i.e., lineages), is the single most important factor explaining participation in self-governing organizations, whose main role is to fill the service provision gap at the grassroots level. In a majority of villages, the centralization of power in local Party organizations has constrained the ability of villagers to exercise “voice” to improve the quality of service provision (Hirschman 1970). At the same time, in villages with active and cohesive lineage groups, villagers can use social sanctions to prevent free-riding and to overcome the “collective action problem” associated with (substitutive) non-state provision. Hence, when state institutions fail to respond to their demands for basic services, villagers in these villages tend to form or join self-governing organizations and to “exit” from state to non-state provision.

By shifting attention from what Tsai (2007ab) calls “encompassing and embedding solidary groups”, and what Lu (2015) calls “indigenous, relation-based institutions”, to what we call self-governing organizations, this study shows that increasing participation in traditional community organizations is not always a source of good governance, but rather a symptom or even a source of poor governance. While these studies argue that the key to good governance in rural China lies in having “the right kind of organizations” i.e., those that bring officials and villagers together (Tsai 2007b: 247), our findings point to the difficulty of having the right kind of organizations without having the “right” kind of government.

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